

VORNADO REALTY TRUST 2002 ANNUAL REPORT



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FINANCIAL HIGHLIGHTS

	Year Ended December 31,	
	2002	2001
Revenues	\$1,435,070,000	\$ 985,773,000
Net income	\$ 209,736,000	\$ 227,233,000
Net income per share — basic	\$ 1.98	\$ 2.55
Net income per share — diluted	\$ 1.91	\$ 2.47
Total assets	\$9,018,179,000	\$6,777,343,000
Shareholders' equity	\$2,627,356,000	\$2,570,372,000
Funds from operations ⁽¹⁾	\$ 407,173,000	\$ 377,693,000

⁽¹⁾ See Management's Discussion and Analysis of Financial Conditions and Results of Operations on page 43 for a reconciliation of net income to funds from operations. Funds from operations does not represent cash generated from operating activities in accordance with generally accepted accounting principles and is not necessarily indicative of cash available to fund cash needs. Funds from operations should not be considered as an alternative to net income as an indicator of the Company's operating performance or as an alternative to cash flows as a measure of liquidity.

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VORNADO COMPANY PROFILE

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ornado Realty Trust is a fully-integrated real estate investment trust. The Company currently owns:

- all or portions of 74 office properties aggregating approximately 27.7 million square feet in the New York City metropolitan area (primarily Manhattan) and in the Washington D.C. and Northern Virginia area;
- 62 retail properties in six states and Puerto Rico aggregating approximately 12.5 million square feet;
- the Merchandise Mart Properties portfolio containing approximately 8.6 million square feet of showroom and office space, including the 3.4 million square foot Merchandise Mart in Chicago;
- a 60% interest in the Vornado Crescent Portland Partnership that owns 88 cold storage warehouses nationwide with an aggregate of approximately 441.5 million cubic feet of refrigerated space leased to AmeriCold Logistics;
- approximately 33.1% of the outstanding common stock of Alexander's, Inc.;
- the Hotel Pennsylvania in New York City consisting of a hotel portion containing approximately 1.0 million square feet with 1,700 rooms and a commercial portion containing 400,000 square feet of retail and office space;
- a 21.7% interest in The Newkirk Master Limited Partnership, which owns office, retail and industrial properties net leased primarily to credit rated tenants, and various debt interests in such properties;
- eight dry warehouse/industrial properties in New Jersey containing approximately 2.0 million square feet; and
- other investments, including interests in other real estate, marketable securities and loans and notes receivable.

Vornado's common shares are listed on the New York Stock Exchange and are traded under the symbol: VNO.

Alexander's common stock is also listed on the New York Stock Exchange and is traded under the symbol: ALX

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TO OUR SHAREHOLDERS

Vornado's Funds From Operations for the year ended December 31, 2002 was \$407.2 million, \$3.62 per diluted share, compared to \$377.7 million, \$3.79 per diluted share, for the year ended December 31, 2001.

Net Income applicable to common shares for the year ended December 31, 2002 was \$209.7 million, \$1.91 per diluted share, versus \$227.2 million, \$2.47 per diluted share, for the previous year. Here are the financial results by segment:

(\$ in millions, except per share data)	% of 2002 Adjusted EBITDA	2002	2001	Same Store
Adjusted EBITDA⁽¹⁾:				
New York Office	33%	303.3	295.2	5.0%
CESCR ⁽²⁾ (34% in 2001)	29%	270.0	84.6	4.1%
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Total Office	62%	573.3	379.8	4.8%
Retail	12%	112.7	119.1	(2.6%)
Merchandise Mart	12%	108.9	110.8	(1.2%)
Temperature Controlled Logistics	8%	71.8	78.4	(8.4%)
Newkirk Joint Venture	8%	69.6	63.4	9.8%
Alexander's	4%	34.4	19.4	77.3%
Hotel Pennsylvania	—	7.6	17.0	(55.3%)
Other (including non-comparable adjustments as detailed below)	(6%)	(57.3)	(2.8)	—
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Total Adjusted EBITDA⁽¹⁾	100%	921.0	785.1	.2%
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Funds From Operations (\$3.62 per share in 2002; \$3.79 per share in 2001)		407.2	377.7	
Adjustments for certain items which affect comparability:				
Primestone foreclosure and impairment losses		35.7	—	
Amortization of officer's employment arrangement		27.5	—	
Gain on sale of non-real estate assets		(18.3)	(15.7)	
Write-offs of non-core investments		6.9	29.1	
Donations to Twin Towers and NYC Fireman's Funds		—	1.3	
Minority interest		(10.6)	(1.8)	
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Funds From Operations, as adjusted (\$3.98 per share in 2002; \$3.92 per share in 2001)		448.4	390.6	

⁽¹⁾ Adjusted EBITDA is defined in Management's Discussion and Analysis of Financial Condition and Results of Operations on page 10 of this Annual Report. Adjusted EBITDA and FFO shown above do not include the benefit of straight-lining of rent and FASB 141 adjustments. See discussion on the next page. Also see reconciliations of these non-GAAP earnings metrics to GAAP Net Income in Management's Discussion and Analysis of Financial Condition and Results of Operations on pages 7-9 and 43 of this Annual Report.

⁽²⁾ Charles E. Smith Commercial Realty.

THE ANTI-REALITY SHOW CALLED ACCOUNTING

Cash flow is the lifeblood of business—ours too. We have long held that Vornado's financial statements should mirror actual cash flow as closely as possible. The accounting profession is making this close to impossible.

In 1976 and 1985, the Financial Accounting Standards Board (FASB) invented and reinvented FASB 13—straight-lining of rents. We write almost all of our leases with contractual rent bumps. FASB 13 requires that the revenue shown in our GAAP financial statements be the average rent for the lease term, not the actual rent received in any given year. Thus, in the early years GAAP revenue is greater than actual cash receipts and the opposite in trailing years. We do this in our GAAP statements because we must. For good or for bad, we had somewhat more flexibility in our FFO⁽¹⁾ reporting. Historically, we have not included the benefit of straight-lining rent when reporting FFO. Only two or three of the 150 companies in our industry make this adjustment, which for us has penalized FFO in recent years by about \$.25 a share, and that's a big penalty.⁽²⁾

In 2001, the FASB brought us FASB 141 and 142. This affects purchase accounting and essentially requires companies to fair value leases for acquisitions completed after July 1, 2001. For us, this affected the Charles E. Smith, Monmouth Mall and Las Catalinas acquisitions, requiring us to recognize in 2002 the present value of below-market leases as a deferred credit to be included into income over the term of the leases. This procedure requires valuations of leases (a cynic would say *subjective* valuations). This non-cash calculation increased our GAAP income in 2002 by \$.08 per share.

We capitulate. With respect to the straight-lining of rents, after years of doing it right, we announced days ago that to comply with the Securities and Exchange Commission's Regulation G (effective March 28, 2003) concerning non-GAAP financial measures, to adhere to NAREIT's definition of FFO and to report FFO for straight-lining of rent on a basis comparable with virtually all other companies in our industry, Vornado will revise its definition of FFO to include the effect of straight-lining of rent. Beginning with the Company's filing of its first quarter 2003 Form 10-Q, the Company will reflect this change retroactively to the earliest period being reported and, accordingly, previously reported FFO per share will be adjusted as follows:

	As Previously Reported	Effect of Change ⁽¹⁾	As Restated
2002	\$3.62	\$.20 ⁽²⁾	\$3.82
2001	\$3.79	\$.21	\$4.00
2000	\$3.45	\$.26	\$3.71

⁽¹⁾ This change eliminates the item for straight-lining of rent in the reconciliation of the non-GAAP earnings metric FFO to GAAP Net Income in Management's Discussion and Analysis of Financial Condition and Results of Operations on page 43 of this Annual Report. A Form 8-K dated April 24, 2003 has been filed with the amended reconciliation.

⁽²⁾ Net of a \$.03 allowance for uncollectible rents.

Similarly, the Company will report FFO including the effect of FASB 141. The Company will reflect this change retroactively to 2002, the Company's effective date for FASB 141, and accordingly, 2002 FFO will increase by \$.09 per share.

⁽¹⁾ FFO (Funds From Operations) is a non-GAAP performance measure universally used by the REIT industry and its investors and analysts. Simply put, FFO is net income plus property depreciation.

⁽²⁾ Investors and analysts who utilize AFFO see through all of this stuff. The acronym AFFO is Adjusted FFO, adjusted for capex, straight-lining and other non-cash items.

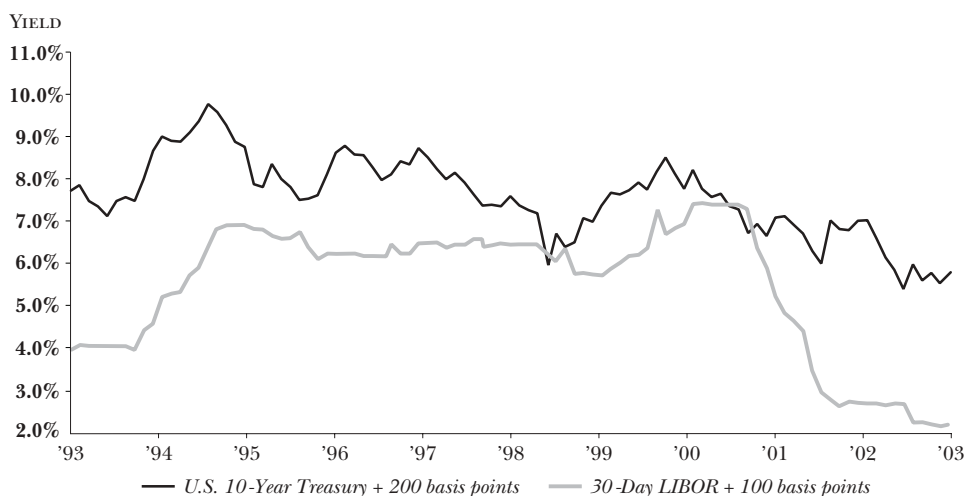
This next item is not accounting per se, but as you will see it involves the same mark to market sort of thing. Green Street⁽³⁾ recently decided to mark down NAVs to reflect its marking of fixed rate debt to market. While this is, of course, intellectually correct, it is ironic. It reinforces our long-held belief that management of the right hand side of the balance sheet is hugely important in creating value. And it disproves the simplistic approach that long-term fixed rate debt is always the safe, value creating way to go.

In a benign interest rate environment, there is as much risk in locking in long term as there is reward. After all, cost of capital is our largest expense item by far. In today's weak market, landlords who are able to avail themselves of low rates can be much more competitive. Those who can't could be slaughtered. Further, it seems to me that the twenty-odd-year bull market in interest rates is still intact.

Here is one of my favorite graphs. It tracks the 10-Year Treasury plus 200 basis points against 30-Day LIBOR plus 100 basis points, surrogates for our long-term and short-term borrowing rates. Interestingly, had you borrowed long, you would have been wrong in all but several months of the last ten years.

Historical Rate Analysis

U.S. 10-Year Treasury + 200 basis points vs. 30-Day LIBOR + 100 basis points



⁽³⁾ Green Street Advisors, "Real Estate Securities Monthly," April 1, 2003.

Vornado's capital structure—the right hand side of the balance sheet—is shown below. The summary balance sheet shown in this table is as at April 23, 2003. It differs from our year-end financial statements by including the Company's pro-rata share of joint venture debt gross and by stating equity at the NYSE closing price of VNO shares on that date.

(\$ in millions except share data)	Amount	Weighted Average Rate
Floating Rate Debt	1,449	2.86%
Fixed Rate Debt	3,642	7.56%
Total Debt (including 1,032 of joint venture debt)	5,091	6.22%
Perpetual Preferred	1,067	8.33%
Market Value of Shares/Units—139.6 million at \$39.52	5,517	N/A
Enterprise Value	11,675	
Debt to Enterprise Value	43.6%	
Debt plus Perpetual Preferred to Enterprise Value	52.7%	

Green Street's mark to market of debt dinged our NAV by \$3 per share. We will do battle over fractions affecting our NAV, but not this time. In fact, Mike and I consider our over-market interest rates to be a hidden asset, valuable, as are our below-market rents. Our income will rise as we refinance above-market debt—and we will gain back that \$3 of NAV over time.

\$500 MILLION UNSECURED DEBT

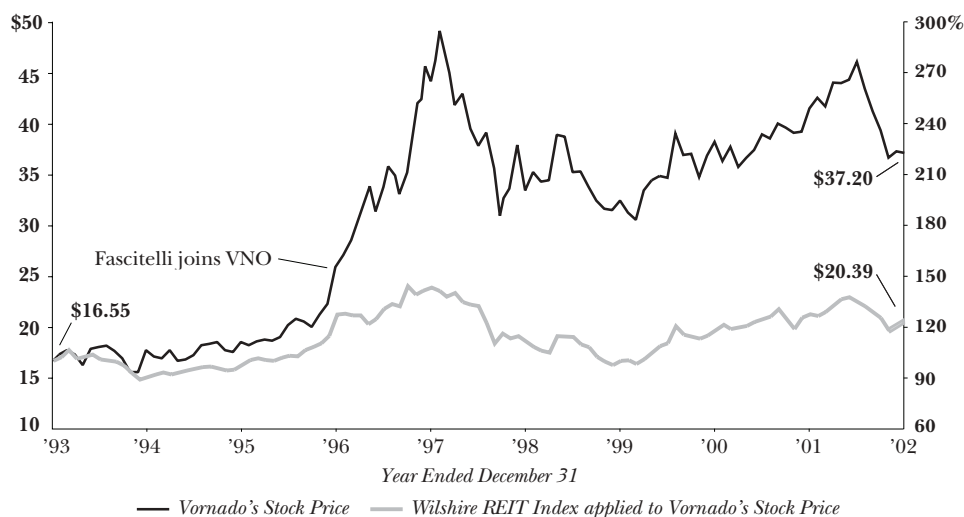
Access to multiple capital markets is the hallmark of a successful company. In June 2002, Vornado was a first-time issuer of unsecured debt, placing \$500 million of five-year 5.66% unsecured notes. These notes were issued at 168 basis points over the five-year treasury, which at the time was 3.98%. Thanks to Wendy for this important deal—and for the as large and as important Hypo deal,⁽⁴⁾ as well.

Mike and I thought we timed this right, but with the 5-Year Treasury today at 2.94% we get a hindsight flunking grade here. But no matter—at issue date we simultaneously swapped this note to floating at 77 basis points over three-month LIBOR in arrears. We are now paying a very satisfactory 2.18% floating rate for this capital. Use of proceeds was to pay off other floating rate debt, leaving our balance sheet both floating rate and leverage neutral. At March 31, 2003, this swap (really the only sizeable derivative on our balance sheet) is in the money by \$35.2 million.

⁽⁴⁾ The \$490 million construction financing for the Alexander's 59th Street tower.

STOCK PERFORMANCE—A VIEW FROM 30,000 FEET

Green Street recently published a report⁽⁵⁾ pointing out what I well know—that our ten-year returns have been extraordinary, our five-year returns have been just ordinary and our one-year return has been negative, and unacceptable. Since we’re all in it for the money, we are totally focused on stock price performance. Here’s a ten-year graph of our stock price versus the Wilshire REIT Index.



Michael Fascitelli joined Vornado as President and chief growth officer in January 1997. The stock celebrated by doubling that year.⁽⁶⁾ In January 1998, Vornado’s stock reached an all-time high of \$49.75 a share, an FFO multiple of 19 and an NAV of \$32.50 per share. In essence, the stock market was discounting the next five years of our growth in Mike’s first year.

Mike has delivered growth in spades. For the record, here’s Adjusted EBITDA and FFO in dollars and per share during the period.

(\$ in millions, except per share data)

Year	Adjusted EBITDA ⁽¹⁾	Funds From Operations ⁽¹⁾		Dividends	
		Per Share	% Increase	Per Share	% Increase
2002	921.0	3.62 ⁽²⁾	(4.5%)	2.66	1.1%
2001	785.1	3.79 ⁽²⁾	9.2%	2.63	33.5%
2000	737.8	3.47	10.2%	1.97	9.4%
1999	609.4	3.15	18.9%	1.80	9.8%
1998	427.1	2.65	108.7%	1.64	20.6%
1997	150.4	1.27 ⁽²⁾	(9.9%)	1.36	11.5%

⁽¹⁾ Reconciliations of the non-GAAP earnings metric FFO to GAAP Net Income for the five years ended December 31, 2002 are in Selected Consolidated Financial Data on page 2 of this Annual Report and the non-GAAP earnings metric Adjusted EBITDA to GAAP Net Income for the three years ended December 31, 2002 are in Management’s Discussion and Analysis of Financial Condition and Results of Operations on pages 7–9 of this Annual Report. Reconciliations for the years in this table not previously mentioned are contained in the appendix to this letter on page 15.

⁽²⁾ Excluding net non-recurring items, 2002 was \$3.98, 2001 was \$3.92 and 1997 was \$1.67 per share.

⁽⁵⁾ Green Street Advisors, “Vornado Realty Trust—What Have You Done For Me Lately?” April 4, 2003.

⁽⁶⁾ Vornado’s stock was \$22.50 on December 2, 1996, the day we announced Mike’s joining. It rose to \$43.44 on September 29, 1997 after a \$7.53 spike the day of the announcement of the AmeriCold acquisition (go figure) and rose to an all-time high of \$49.75 on January 20, 1998.

As a regulated REIT, we pay out 100% of our taxable income as dividends. Our intention is to pay out no more. Our dividends, when combined with capex, leave little over in the form of retained earned capital. While I can't think of anything better than paying out our earnings to our shareholders, myself and all my partners, in the larger sense it means that we must sell new shares in order to grow. We have done so repeatedly. Since January 1997, we have sold over 46.3 million shares in 6 separate offerings at an average price of \$41.41 per share gross.⁽⁷⁾ We seem to have conditioned the market to expect a share issuance whenever the share price gets to the mid \$40s. We will issue shares only when we get at least as much or more value than we give.

Should we reverse course and buy back shares? We know how to do this. In the 1980s, Vornado implemented one of the largest cap shrinks in the history of the NYSE, buying back 60% of its shares. But that was done at deep discounts of 50% or more to underlying value. In the modern era, we have not done buybacks, although this is a value-enhancing technique that we would use, and use in scale, in the right circumstances. Any buyback over the last two years would have been only slightly accretive to FFO and NAV. Source of funds is the key here. To the extent we have excess cash flow, buybacks so funded would be perfect. Buybacks from sale proceeds would be acceptable, but would yield marginally more than merely trading water. Buybacks from borrowings are a narcotic we will avoid.

We have been an asset accumulator, growing in the absolute. We have sold a few small odds and ends—nothing really. Several shareholders and analysts have suggested that we have grown to be too big, that the growth rate per share we seek cannot be achieved on such a large asset base (at least in this market) and that it's about time we became an asset recycler. We have well over \$1 billion in profits in our New York office assets alone that we could harvest. Our goal is definitely to sell assets this year.

The selection of which assets to sell is easy. Those that we would re-acquire at current market prices are keepers. All others are candidates for sale. The best candidates are those that we no longer wish to own for whatever reason or where we are offered an outsized price.

There are ramifications to selling assets. Without rapid redeployment of the proceeds, selling assets is dilutive. Selling assets creates (hopefully) capital gains tax issues that can either be handled through like-kind exchanges (sort of like swapping my cats for your dogs) or capital gains dividend distributions (i.e., shrinking the company).⁽⁸⁾ Mike and I have a lot to think about in this regard.

⁽⁷⁾ We have also issued 39.9 million Operating Partnership Units (principally for the Mendik, Merchandise Mart and Smith acquisitions) at an average price per unit of \$38.39.

⁽⁸⁾ The private real estate market functions differently here. As buildings appreciate over time, the private owner shuns selling and paying taxes in favor of the non-recourse loan—mortgaging and re-mortgaging again and again, realizing excess financing proceeds on a tax-free basis. Now that's the ticket.

LEASE, LEASE, LEASE

Everyone knows business is soft. It seems like every business in America is contracting, although the rate of contraction seems to be slowing. Our mission during these times is the same as always—and that is to lease, lease, lease. Here's the math.

	Office		Retail	Merchandise Mart	
	New York	CESCR		Office	Showroom
Year Ended December 31, 2002:					
Square feet leased (in thousands)	579	2,342	1,960	164	911
Initial rent per square foot	\$44.34	\$31.29	\$12.17	\$26.97	\$18.99
Percentage increase ⁽¹⁾	30.0%	5.5%	32.4%	1.2%	2.0%
Occupancy rate	95.9%	93.6%	88.3%	91.7%	95.2%
Quarter Ended March 31, 2003:					
Square feet leased (in thousands)	235	563	110	101	436
Initial rent per square foot	\$43.86	\$31.27	\$27.03	\$23.15	\$22.62
Percentage increase ⁽¹⁾	30.5%	5.6%	17.6%	5.8%	21.4%
Occupancy rate	95.9%	93.2%	87.5%	92.7%	95.3%

⁽¹⁾ *Percentage increase over expiring escalated rent.*

In this market, David Greenbaum has maintained 96% occupancy in New York—think about that. In first quarter 2003, his roll over rents increased 30.5%—think about that. In the school of New York real estate, David is a dean. Chris Kennedy's showroom results continue to be extraordinary, as well.

All leasing markets continue to challenge. Our capex for tenant improvements is up,⁽⁹⁾ and while we always lease more than our share, we are budgeting occupancies and rents conservatively for the rest of this year.

⁽⁹⁾ . . . but not as much as was estimated for 2003 outlays in the MD&A in our 2002 financials. Revised estimates will be included in our first quarter 2003 financials to be filed shortly.

BMS

In 1997, when we acquired the Mendik Company, the cornerstone of our New York City office business, Bernie Mendik and his partners held on to Building Maintenance Service Company (BMS), the company that provides cleaning, security and engineering services to the buildings we bought then, as well as to buildings we would acquire over the next ten years. In a deal completed on January 1, 2003, we acquired BMS for \$13 million. This is actually a big business, with 1,150 employees, \$82 million in revenue and \$5-ish million of bottom line. We will seek to grow this business by providing cleaning services to our malls and perhaps even to our other office assets.

CESCR/KAEMPFER

On January 2, 2002, we completed the acquisition of the 66% of CESCR that we didn't already own. We now own 100%. Bob Smith and Bob Kogod, the partners and brothers-in-law who over the last fifty years built this business into the largest office landlord in the Washington, D.C. area, continue to be actively involved in management—and we want them to be. Months ago we began an external search⁽¹⁰⁾ for a candidate for President. We had very specific requirements for this position, most importantly, that he/she be Washington-based with extensive knowledge of the Washington market, its brokers, its tenants, etc. The best candidate by far was Mitchell Schear, and Mike and I am delighted he is now division head of the Charles E. Smith Company.

Mitchell is a seasoned 44 year old real estate executive with unique leasing and development skills. Mitchell also came with a dowry. As Mike was courting Mitchell, who at the time was president of the Kaempfer Company, the best arrangement for all turned out to be our acquisition of Kaempfer. We got Mitchell, sliver interests in six important District of Columbia buildings and, importantly, the Kaempfer management company with its long-term management and leasing fees. Mitchell is now working closely with Bob Smith, Ken McVeary and Brent Bitz to make this great company even greater.

⁽¹⁰⁾ *We have been hugely successful with external searches for division heads, witness Mel Blum, Alec Covington and Sandeep Mathrani.*

RETAIL

It occurs to me that I have spent the last ten years diversifying away from retail.⁽¹¹⁾ I am keenly aware that over the last year or two the stock market has awarded retail the highest marks by far.⁽¹²⁾ The miscalculation I made here was underrating the great American consumer and not anticipating that lifetime low interest rates would fuel consumer buying and buying. But beware, retail saturation and over-storing will create dangers that over time only skilled managements will be able to avoid.

Retail is a core business of Vornado. In fact, it is our original business, the business we grew up in. A baseball manager shapes his team based upon the talents and strengths of his players. We have a proven star player in Sandeep Mathrani. Vornado will be growing in retail.

Don't be fooled by the 2002 decline in retail Adjusted EBITDA, same store and occupancy, which were caused largely by several bankruptcies and the in-process repositioning of the Bradlees centers. Sandeep, Sherri and the retail leasing team are on fire. Our internal projections are that retail will be our number one grower in 2003 and 2004.

Hotel Pennsylvania is suffering. Its solution lies in big box retail at the base and a repositioning. All this will require patience and better markets.

⁽¹¹⁾ *We have grown our retail business, just not quite as fast as our office business. After all, we did acquire the Green Acres super regional mall, 50% of the Monmouth mall, two regional malls in Puerto Rico, etc.*

⁽¹²⁾ *No sour grapes here. No investment, not retail, not anything, has done better than our New York office acquired at \$175 per foot.*

PEOPLE

Alec Covington is a great manager who has worked hard to stabilize AmeriCold. We have said repeatedly and publicly that AmeriCold's performance has been a disappointment.⁽¹³⁾ We will restructure the leases with AmeriCold this year. We will re-double our efforts to withdraw capital here.

In 1998, Vornado acquired the Chicago Merchandise Mart, Chris Kennedy's family business. Chris Kennedy has worked in this business for 16 years and in October 2000 was promoted to division head of our Mart business. Chris is talented and uniquely qualified to run this business, which has over \$100 million of EBITDA and \$1 billion of assets.

Joe Hakim, who had run the Mart business for the last ten years, has retired. Mike, Chris and I hold Joe in the highest regard and thank him for all he did for us. We wish Karen good health. We're certain that our young friend Joe (54) has one more career in front of him.

Paul Larner was CFO and then Chief Operating Officer of CESC. This year we were lucky enough to convince Paul to move up to New York / New Jersey as EVP—Chief Administrative Officer of Vornado.

Michelle Felman, EVP and acquisitions division head, pulled off one miracle this year and her usual quota of other deals. She is a strong advocate with great judgment—especially at those times this year when she was the lone voice.

⁽¹³⁾ *But not a tragedy. After the disappointments and declines, the business still returned 10.3% on our leveraged capital in 2002.*

CORPORATE GOVERNANCE

A very few, very dishonest executives have created havoc in the investing community. Congress, the stock exchange and analysts (who for sure are not blameless) have focused on the independent board of directors as the cure all. I believe an independent board is absolutely, absolutely necessary. But while an independent board is surely necessary, it is not a sufficient solution.

Independent directors, however capable, are not sufficient to stop abuses. In my mind, the single most important corporate governance item is *total* disclosure, the information that allows investors to understand all the workings and all the details of a company's business. It is this objective toward which Joe, Ross, Matt and our financial team strive. Our 168-page and growing 10K (with its 39-page MD&A) is a huge step towards this continuing objective. Our new 61-page supplemental package is another. Each quarter and each year our filings contain more and more disclosure. This trend will continue.

Vornado's incumbent nine-member Board is uniquely qualified to oversee our business by virtue of their business savvy and in the case of seven members, their nine-figure investments in Vornado. They always ask the challenging questions. Vornado will enthusiastically increase its board so that a majority of directors are independent. We'll need to attract a handful of truly qualified new independent directors, and we will. This will take time.

In May 2002, a non-binding precatory shareholder proposal to declassify Vornado's staggered Board was carried 51% to 49%. After deliberation and external advice, Vornado's Board determined to maintain the staggered format. In fact, we inherited a staggered board. Historians may remember that over twenty years ago current management took over the Company—and it took proxy contests at two annual meetings to do so. Our belief that a staggered Board is appropriate is not self-serving or entrenching—this is a big business and stability and continuity are important.

Vornado's proxy, filed with this annual report, discloses a change in stock-based compensation favoring restricted share grants in lieu of options. Unfortunately, this seems to be becoming industry standard.

SIGHTSEEING

Shareholders may wish to inspect our recently completed buildings and our under construction projects and follow their progress. First in the New York area.

Vornado is the for-fee, ground up developer of 731 Lexington Avenue (at 59th Street)—the Bloomberg Tower—on behalf of our one-third owned affiliate, Alexander's. This Cesar Pelli masterpiece is rising quickly. Steel is erected to the 30th floor and curtain wall is following on pace. First delivery to our principal tenant will occur in late fall 2003, with completion expected in 2005. This building will have retail at the base, 700,000 square feet for Bloomberg, 183,000 square feet of additional office and 105 condominium residences. If shareholders would like to eat their own cooking, please visit the residential sales office—the apartments will be stunning.

Steel and curtain wall are going up at 640 Fifth Avenue (at 51st Street), where we are filling out the wedding cake by adding 47,000 square feet. Here, we will create some of the very finest office space in Manhattan overlooking the gardens of Rockefeller Center and the spires of St. Patrick's Cathedral. Three years ago, at the base of this same building, we created Hennes & Mauritz's U.S. flagship.

Scaffolding will go up within the month signaling the beginning of the re-development of the former Bradlees store at 4 Union Square South (14th Street). Sandeep has already completed retail deals here with Whole Foods and Forever 21 aggregating 73,000 square feet, which accounts for the most valuable one-third of this building.

In October, we delivered a newly built 43,000 square foot store at 34th Street and 7th Avenue to Hennes & Mauritz. This building also serves as a sign tower, hosting the first two giant display signs erected under our special 34th Street signage district.

All these are projects of our development division headed by Mel Blum and involved the collaboration of David and Sandeep for leasing. Mike and I recognize their talents and we thank them all.

In Washington, please visit Crystal City, the flagship asset of CESC. Mike and I believe in the future of this 26 building, 7.4 million square foot complex literally contiguous to Washington's Reagan National Airport, close by the Pentagon. Here, Bob Smith, Mitchell and the team are in the first phase of construction of a new urban streetscape with retail, restaurants and entertainment venues. With road and traffic improvements, Crystal Drive will become an urban boulevard. This \$42 million project will add considerable value.

WIN, LOSE OR DRAW

- Rents have now declined to the point where it is uneconomic to manufacture new real estate. This is a huge positive for Vornado's existing assets.
- Real estate is a stable, sound investment that has out-performed all of the major indices, including the S&P 500, NASDAQ, the Russell 2000 and the Dow, for the one, three, five and ten-year periods ended December 31, 2002.⁽¹⁴⁾ Recognition of this by investors will cause a re-pricing of public real estate from being under-valued to fair value and maybe even a bit more.
- Cap rates have come in. Low interest rates will be with us long enough to draw cap rates down even further. Real estate may still be cheap here.
- Vornado is a great current investment, but Vornado may be an even better warrant on future appreciation. Think about these numbers: a \$50 per square foot increase in New York values creates \$5 per share of shareholder value; \$5 per square foot of incremental net rent in Washington creates about \$750 million of shareholder value over time as leases roll.
- My father, now 86, taught me that if you have no bad debts you're not making enough sales. The analogy here is that we do make mistakes, but our mistakes are few and smallish in relation to our business. When we make a mistake it is painfully, publicly and quickly disclosed.⁽¹⁵⁾
- Asking rents in New York went from \$13 per square foot in 1970, to \$24 in 1980, to \$33 in 1990, to \$55 in 2000. While the ascent has not been linear, the message is clear—the passage of time is our biggest ally in value building (and I don't mean a quarter or two). And our shareholders get 7% while waiting.

Mike and I are learning that simplicity is a virtue.



Steven Roth
Chairman

April 23, 2003

⁽¹⁴⁾ I am the 2002—2003 Chair of NAREIT and this is my commercial for our industry. Moreover, it's absolutely, factually correct.

⁽¹⁵⁾ We made a mistake in the Primestone matter. It is now behind us. (By the way, we made a second investment here, providing mezzanine financing to Prime Group Realty Trust's Dearborn Center project as part of a bank group. Our \$23.4 million investment was repaid in full on March 19, 2003, together with look-back interest resulting in a 23% yield to us over the life of the investment.)

APPENDIX

Below is a reconciliation of Net Income to Adjusted EBITDA:

<i>(\$ in millions)</i>	<i>1999</i>	<i>1998</i>	<i>1997</i>
<i>Net income</i>	<i>202.5</i>	<i>152.9</i>	<i>61.0</i>
<i>Minority interest</i>	<i>55.0</i>	<i>16.2</i>	<i>7.3</i>
<i>Interest and debt expense</i>	<i>226.3</i>	<i>164.4</i>	<i>54.4</i>
<i>Depreciation and amortization</i>	<i>143.5</i>	<i>104.3</i>	<i>32.0</i>
<i>Net gain from insurance settlement and condemnation proceeding</i>	<i>—</i>	<i>(9.6)</i>	<i>—</i>
<i>Straight-lining of rents</i>	<i>(25.4)</i>	<i>(16.1)</i>	<i>(3.9)</i>
<i>Other</i>	<i>7.5</i>	<i>15.0</i>	<i>(0.4)</i>
<i>Adjusted EBITDA</i>	<i>609.4</i>	<i>427.1</i>	<i>150.4</i>

Below is a reconciliation of Net Income to Funds from operations:

<i>(\$ in millions)</i>	<i>1997</i>
<i>Net income</i>	<i>45.5</i>
<i>Depreciation and amortization of real property</i>	<i>22.4</i>
<i>Straight-lining of rents</i>	<i>(3.4)</i>
<i>Leasing fees received in excess of income recognition</i>	<i>1.7</i>
<i>Proportionate share of adjustments to equity in income of partially-owned entities to arrive at funds from operations:</i>	
<i>Temperature Controlled Logistics</i>	<i>4.2</i>
<i>Alexander's</i>	<i>(2.5)</i>
<i>Partially-owned office buildings</i>	<i>2.9</i>
<i>Hotel Pennsylvania</i>	<i>0.5</i>
<i>Charles E. Smith Commercial Realty L.P.</i>	<i>1.3</i>
<i>Funds from operations</i>	<i>72.6</i>

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PROPERTIES

Vornado Realty Trust

LOCATION	SQUARE FEET	PERCENT LEASED	PRINCIPAL TENANTS
OFFICE PROPERTIES			
NEW YORK (MANHATTAN)			
One Penn Plaza ⁽¹⁾	2,509,000	96.7%	Buck Consultants, Cisco Systems, First Albany, General Motors Acceptance Corp., Kmart, MWB Leasing, Parsons Brinkerhoff, Public Service Commission, Stone & Webster, United States Customs Department
Two Penn Plaza	1,525,000	95.4%	Compaq Computer, Forest Electric, Information Builders, Inc., Madison Square Garden, McGraw Hill Co., Inc., US Healthcare Service
909 Third Avenue ⁽¹⁾	1,305,000	96.2%	Bear Stearns, Citibank, Fischbein Badillo, Forest Laboratories, Ogilvy Public Relations, Shearman & Sterling, U.S. Post Office, Wiley Publishing
770 Broadway	1,046,000	99.6%	J. Crew, Kmart, VIACOM International Inc., V.N.U. U.S.A, Inc.
Eleven Penn Plaza	1,024,000	97.0%	McCall Pattern Company, EMC Corp., Executive Office Network, Faulkner & Gray, Federated Department Stores, General Media, Rainbow Media Holdings
Two Park Avenue	964,000	98.6%	Hartford Insurance, Herrick Feinstein, Medical Liability Mutual Ins, Schiefflin & Somerset, Tribune Company, United Way
90 Park Avenue	890,000	92.9%	Sterling Winthrop Inc., Warnaco, Alston & Bird
888 Seventh Avenue ⁽¹⁾	877,000	92.1%	Arista Records, New Line Realty, Soros Fund, Kaplan Educational Center, The Limited
330 West 34th Street ⁽¹⁾	637,000	99.9%	City of New York, Props for Today, The Bank of New York
1740 Broadway	567,000	99.8%	Davis & Gilbert, Dept. of Taxation of the State of N.Y., Mutual Life Insurance, William Douglas McAdams
150 East 58th Street ⁽¹⁾	559,000	88.8%	
866 United Nations Plaza	391,000	98.1%	Fross Zelnick, Mission of Japan, The United Nations
595 Madison (Fuller Building)	305,000	91.4%	
640 Fifth Avenue	268,000	99.4%	Weber Shandwick Worldwide
40 Fulton Street	238,000	85.4%	
689 Fifth Avenue	89,000	74.3%	
7 West 34th Street	424,000	100.0%	Fairchild Publications Inc., Health Insurance Plan of NY
330 Madison Avenue (25% Interest)	784,000	88.8%	Bank Julius Baer, BDO Seidman
20 Broad Street (60% Interest) ⁽¹⁾	466,000	93.6%	N.Y. Stock Exchange
825 Seventh Avenue (50% Interest)	165,000	100.0%	Young & Rubicam
New Jersey			
Paramus ⁽¹⁾	128,000	91.7%	Vornado's Administrative Headquarters
Total New York City Office Buildings	15,161,000	95.6%	
Vornado's Ownership Interest	14,304,000	95.9%	

LOCATION	SQUARE FEET	PERCENT LEASED	PRINCIPAL TENANTS
WASHINGTON, DC AND NORTHERN VIRGINIA			
Crystal Mall	1,066,000	98.9%	General Services Administration
Crystal Plaza	1,226,000	99.2%	General Services Administration
Crystal Square	1,386,000	97.9%	General Services Administration, Lockheed Martin, Oblon Spivak, Batella Memorial Institute
Crystal Gateway	1,443,000	94.4%	Boeing, General Services Administration
Crystal Park	2,160,000	97.0%	CESCR Headquarters, General Services Administration, Archstone Smith, Anteon, US Airways Headquarters, Boeing
Arlington Plaza	173,000	86.5%	Science Research Analysis Corp.
1919 S. Eads Street	96,000	87.6%	General Dynamics
Skyline Place	2,016,000	86.6%	General Services Administration
One Skyline Tower	476,000	100.0%	General Services Administration
Courthouse Plaza ⁽¹⁾	615,000	99.1%	Arlington County
1101 17th Street	205,000	87.5%	American Federation of States
1730 M Street ⁽¹⁾	189,000	92.1%	MHI DC Inc.
1140 Connecticut Avenue	175,000	91.5%	National Legal Aid
1150 17th Street	225,000	95.6%	American Enterprise Institute, Unisys Corp
1750 Pennsylvania Avenue	262,000	97.9%	General Services Administration, PA Consulting Group Holdings
Democracy Plaza I ⁽¹⁾	207,000	98.0%	National Institute of Health
Tysons Dulles	473,000	89.6%	Keane Federal Systems, Inc.
Commerce Executive	413,000	56.0%	BT North America
Reston Executive	484,000	93.5%	Science Applications Int'l Corp.
Fairfax Square (20% interest)	105,000	83.6%	Cineplex Odeon, Platinum Technologies, Ernst & Young
Total Washington, DC and Northern Virginia Office Buildings	13,395,000	93.6%	
Total Office Properties	28,556,000		
Vornado Ownership Interest	27,699,000		



LOCATION	SQUARE FEET	PERCENT LEASED	PRINCIPAL TENANTS
RETAIL PROPERTIES			
NEW JERSEY			
Bordentown	179,000	95.0%	Shop-Rite
Bricktown	263,000	95.7%	Kohl's, Foodrama Shop-Rite
Cherry Hill	295,000	70.6%	Toys "R" Us
Delran	172,000	100.0%	Sam's Wholesale
Dover	173,000	98.7%	Shop-Rite, Lowe's Home Center ⁽²⁾
East Brunswick	231,000	100.0%	Kohl's, T.J. Maxx, Circuit City, Dick's Sporting Goods
East Hanover I	271,000	97.6%	Home Depot, Dick's Sporting Goods, Marshalls
East Hanover II	77,000	99.2%	
Hackensack	269,000	100.0%	Home Depot, Pathmark, Staples
Jersey City	225,000	95.7%	Shop-Rite, Lowe's Home Center ⁽²⁾
Kearny	106,000	100.0%	Pathmark, Marshalls
Lawnside	145,000	100.0%	Home Depot, Drug Emporium
Lodi	171,000	100.0%	National Wholesale Liquidators
Manalapan	198,000	57.2%	Best Buy, Bed Bath & Beyond
Marlton	181,000	86.6%	Kohl's, Shop-Rite
Middletown	232,000	91.9%	Kohl's, Stop & Shop
Monmouth Mall (50% interest)	743,000	96.3%	Boscov's ⁽³⁾ , JC Penney ⁽³⁾ , Loews Theatre, Lord & Taylor, Old Navy, Macy's ⁽³⁾
Morris Plains	177,000	100.0%	Kohl's, Shop-Rite
North Bergen	62,000	100.0%	Waldbaum's
North Plainfield ⁽¹⁾	219,000	89.9%	Kmart, Pathmark
Totowa	317,000	100.0%	Bed Bath & Beyond, Home Depot, Marshalls
Turnersville	96,000	100.0%	Haynes Furniture
Union	263,000	82.6%	Toys "R" Us, Lowe's Home Center ⁽²⁾
Vineland	143,000	5.6%	
Watchung	166,000	98.2%	B.J.'s Wholesale
Woodbridge	235,000	50.9%	A&P, Syms
NEW YORK			
Manhattan:			
1135 Third Avenue	25,000	100.0%	
4 Union Square South (in development)	230,000		Whole Foods ⁽²⁾ , Forever 21 ⁽²⁾
424 Sixth Avenue	10,000	100.0%	
435 Seventh Avenue	43,000	100.0%	Hennes & Mauritz
484 Eighth Avenue	14,000	100.0%	TGI Friday's
715 Lexington Avenue	32,000	72.3%	
825 Seventh Avenue	3,000	100.0%	
OTHER:			
Albany (Menands)	140,000	74.0%	Fleet Bank, State of N.Y.
Buffalo (Amherst) ⁽¹⁾	297,000	81.1%	Circuit City, Media Play, Toys "R" Us, T.J. Maxx
Freeport	167,000	100.0%	Home Depot, Cablevision

LOCATION	SQUARE FEET	PERCENT LEASED	PRINCIPAL TENANTS
New Hyde Park ⁽¹⁾	101,000	100.0%	Stop & Shop
North Syracuse	98,000	100.0%	Reisman Properties
Rochester	205,000	100.0%	Wal-Mart
Rochester (Henrietta) ⁽¹⁾	148,000	0.0%	
Valley Stream (Green Acres) ⁽¹⁾	1,596,000	97.1%	Macy's, Sears, National Wholesale Liquidators, Washington Mutual, Circuit City, GreenPoint Bank, Wal-Mart
PENNSYLVANIA			
Allentown	621,000	98.1%	Shop-Rite, Burlington Coat Factory, Wal- Mart, Sam's Wholesale, T.J. Maxx
Bensalem	126,000	98.4%	Kohl's
Bethlehem	159,000	74.4%	Giant Food Stores, Super Petz
Broomall	169,000	100.0%	Giant Food Stores
Glenolden	102,000	10.1%	
Lancaster	228,000	93.6%	Weis Markets, Lowe's Home Center
Levittown	105,000	100.0%	Haynes Furniture
10th and Market Streets, Philadelphia	271,000	73.7%	Kmart
Upper Moreland	122,000	100.0%	Sam's Wholesale
York	111,000	24.6%	
MARYLAND			
Baltimore (Towson)	152,000	79.3%	Staples, Basics
Baltimore (Dundalk)	184,000	81.9%	A&P, Ollie's
Glen Burnie	121,000	100.0%	Weis Markets
Hagerstown	149,000	35.5%	Big Lots
CONNECTICUT			
Newington	183,000	100.0%	Wal-Mart
Waterbury	146,000	64.8%	Price Chopper
MASSACHUSETTS			
Chicopee	116,000	100.0%	Wal-Mart ⁽²⁾
Milford ⁽¹⁾	83,000	100.0%	Kohl's
Springfield	125,000	100.0%	Wal-Mart
PUERTO RICO (SAN JUAN)			
Montehiedra Mall	554,000	91.8%	Kmart, Home Depot, Marshalls, Caribbean Theatres
Las Catalinas Mall	354,000	96.6%	Kmart
Total Shopping Centers	12,899,000	88.8%	
Vornado's Ownership Interest	12,528,000	88.3%	



LOCATION	SQUARE FEET	PERCENT LEASED	PRINCIPAL TENANTS
WAREHOUSE/INDUSTRIAL PROPERTIES			
NEW JERSEY			
East Brunswick	326,000	71.7%	
East Hanover	942,000	100.0%	
Edison	272,000	100.0%	
Garfield	487,000	100.0%	
Total Warehouse	2,027,000	95.3%	
MERCHANDISE MART PROPERTIES			
ILLINOIS			
Merchandise Mart, Chicago	3,435,000	94.9%	Baker, Knapp & Tubbs, Bankers Life & Casualty, CCC Information Services, Chicago Teachers Union, Chicago Transit Authority, Holly Hunt Ltd., Hon Industries, Navtech, Office of the Special Deputy Receiver, Beacon Hill/Masco, Steelcase, TFA/Leo Burnett Technology LLC
350 North Orleans, Chicago	1,149,000	83.8%	21st Century Telecom/RCN, Ameritech, Art Institute of Illinois, Bank of America, Chicago Transit Authority, Fox Sports, Fiserv Solutions
33 North Dearborn Street, Chicago	325,000	88.2%	
Other	19,000	76.7%	
WASHINGTON, D.C.			
Washington Office Center	396,000	98.7%	General Services Administration
Washington Design Center	388,000	96.4%	
Other	93,000	62.0%	
HIGH POINT, NORTH CAROLINA			
Market Square Complex	2,006,000	99.4%	Cambium Business, Century Furniture Company, La-Z-Boy, Progressive Furniture, Robinson & Robinson
CALIFORNIA			
L.A. Mart	757,000	86.7%	
Total Merchandise Mart Properties	8,568,000	93.6%	
Grand Total	52,050,000		
Grand Total Vornado's Ownership Interest	50,822,000		

⁽¹⁾ 100% ground and/or building interest, other than 150 East 58th Street and Green Acres, where approximately 10% of the ground is leased.

⁽²⁾ Lease has not commenced.

⁽³⁾ Tenant owns land and building.

Alexander's Properties
(A 33.1% Owned Investment)

LOCATION	SQUARE FEET	PERCENT LEASED	PRINCIPAL TENANTS
OPERATING PROPERTIES			
NEW YORK			
Kings Plaza Regional Shopping Center—Brooklyn	759,000	98%	Sears
Rego Park I—Queens	351,000	100%	Bed Bath & Beyond, Circuit City, Marshalls, Sears
Flushing—Queens	177,000	—	
NEW JERSEY			
Paramus—New Jersey	—	100%	IKEA
	1,287,000		
DEVELOPMENT PROPERTIES			
New York:			
59th Street and Lexington Avenue—Manhattan	1,297,000	—	Bloomberg, L.P., Hennes & Mauritz
Rego Park II—Queens		—	

The Newkirk Master Limited Partnership
(A 21.7% Owned Investment)

The Newkirk Limited Partnership owns an aggregate of 19.6 million square feet of office, retail and industrial properties located throughout the United States, which are net leased primarily to credit rated tenants.

Temperature Controlled Logistics
(A 60% Owned Investment)

The Temperature Controlled Logistics business owns 88 refrigerated warehouses with an aggregate capacity of approximately 441.5 million cubic feet. The warehouses are located in 32 states.

TABLE OF CONTENTS

Selected Consolidated Financial Data	1
Management's Discussion and Analysis of Financial Condition and Results of Operations	3
Consolidated Balance Sheets	53
Consolidated Statements of Income	54
Consolidated Statements of Shareholders' Equity	55
Consolidated Statements of Cash Flows	57
Notes to Consolidated Financial Statements	58
Independent Auditors' Report	99
Market Price of Vornado Common Stock and Related Information	100
Vornado Corporate Information	102

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SELECTED CONSOLIDATED FINANCIAL DATA

Vornado Realty Trust

Year Ended December 31,

(in thousands, except share and per share amounts)	2002 ⁽²⁾	2001 ⁽²⁾	2000	1999	1998
Operating Data					
Revenues:					
Rentals	\$ 1,248,903	\$ 841,999	\$ 695,078	\$ 591,270	\$ 425,496
Expense reimbursements	159,978	133,114	120,056	96,842	74,737
Other income	26,189	10,660	10,838	8,251	9,627
Total Revenues	1,435,070	985,773	825,972	696,363	509,860
Expenses:					
Operating	541,596	398,969	318,360	282,118	207,171
Depreciation and amortization	205,826	123,862	99,846	83,585	59,227
General and administrative	98,458	72,572	47,911	40,151	28,610
Amortization of officer's deferred compensation expense	27,500	—	—	—	—
Costs of acquisitions and development not consummated	6,874	5,223	—	—	—
Total Expenses	880,254	600,626	466,117	405,854	295,008
Operating Income	554,816	385,147	359,855	290,509	214,852
Income applicable to Alexander's	29,653	25,718	17,363	11,772	3,123
Income from partially-owned entities	44,458	80,612	86,654	78,560	32,025
Interest and other investment income	31,685	54,385	32,926	18,359	24,074
Interest and debt expense	(239,525)	(173,076)	(171,398)	(141,683)	(114,686)
Net (loss) gain on disposition of wholly-owned and partially- owned assets other than real estate	(17,471)	(8,070)	—	—	9,649
Minority interest:					
Perpetual preferred unit distributions	(72,500)	(70,705)	(62,089)	(19,254)	(756)
Minority limited partnership earnings	(64,899)	(39,138)	(38,320)	(33,904)	(14,822)
Partially-owned entities	(3,185)	(2,520)	(1,965)	(1,840)	(605)
Income before gains on sales of real estate and cumulative effect of change in accounting principle	263,032	252,353	223,026	202,519	152,854
Gains on sale of real estate	—	15,495	10,965	—	—
Cumulative effect of change in accounting principle	(30,129)	(4,110)	—	—	—
Net income	232,903	263,738	233,991	202,519	152,854
Preferred share dividends	(23,167)	(36,505)	(38,690)	(33,438)	(21,690)
Net income applicable to common shares	\$ 209,736	\$ 227,233	\$ 195,301	\$ 169,081	\$ 131,164
Income per share — basic	\$ 1.98	\$ 2.55	\$ 2.26	\$ 1.97	\$ 1.62
Income per share — diluted	\$ 1.91	\$ 2.47	\$ 2.20	\$ 1.94	\$ 1.59
Cash dividends declared for common shares	\$ 2.66	\$ 2.63	\$ 1.97	\$ 1.80	\$ 1.64
Balance Sheet Data					
Total assets	\$9,018,179	\$6,777,343	\$6,403,210	\$5,479,218	\$ 4,425,779
Real estate, at cost	7,559,694	4,690,211	4,354,392	3,921,507	3,315,891
Accumulated depreciation	737,426	506,225	393,787	308,542	226,816
Debt	4,071,320	2,477,173	2,688,308	2,048,804	2,051,000
Shareholders' equity	2,627,356	2,570,372	2,078,720	2,055,368	1,782,678

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SELECTED CONSOLIDATED FINANCIAL DATA *continued*

Vornado Realty Trust

(in thousands)	Year Ended December 31,				
	2002 ⁽²⁾	2001 ^{(2) (3)}	2000 ⁽³⁾	1999	1998
Other Data					
Funds from operations ⁽¹⁾ :					
Net income applicable to common shares	\$ 209,736	\$ 227,233	\$ 195,301	\$ 169,081	\$ 131,164
Cumulative effect of change in accounting principle	30,129	4,110	—	—	—
Depreciation and amortization of real property	195,808	119,568	97,744	82,216	58,277
Straight-lining of property rentals for rent escalations	(27,295)	(24,314)	(28,893)	(22,881)	(14,531)
Amortization of below market leases, net	(12,634)	—	—	—	—
Leasing fees received in excess of income recognized	1,318	1,954	1,259	1,705	1,339
Net gain on sale of real estate	—	(12,445)	(10,965)	—	—
Net gain from insurance settlement and condemnation proceedings	—	(3,050)	—	—	(9,649)
Appreciation/ (depreciation) of securities held in officer's deferred compensation trust	—	3,023	4,765	(340)	340
Gains on sale of securities available for sale	—	—	—	(383)	(898)
Proportionate share of adjustments to equity in income of partially-owned entities to arrive at funds from operations: Temperature Controlled Logistics	36,500	34,531	35,565	31,400	41,988
Alexander's	(2,825)	(5,980)	93	1,324	4,023
Partially-owned office buildings	2,847	1,913	2,926	50	3,561
Hotel Pennsylvania	—	—	5,779	4,866	4,083
Charles E. Smith Commercial Realty L.P.	—	17,917	15,767	12,024	2,974
Other	12,763	10,538	9,448	7,463	219
Minority interest in partially owned entities in excess of preferential distributions	(45,324)	(16,810)	(16,445)	(9,020)	(3,991)
Dilutive effect of Series A Preferred Share dividends	6,150	19,505	21,689	16,268	—
Funds from operations⁽¹⁾	\$ 407,173	\$ 377,693	\$ 334,033	\$ 293,773	\$ 218,899
Cash flow provided by (used in):					
Operating activities	\$ 499,825	\$ 387,685	\$ 249,921	\$ 176,895	\$ 189,406
Investing activities	(24,117)	(79,722)	(699,375)	(494,204)	(1,257,367)
Financing activities	(533,092)	(179,368)	473,813	262,131	879,815

⁽¹⁾ Funds from operations does not represent cash generated from operating activities in accordance with accounting principles generally accepted in the United States of America and is not necessarily indicative of cash available to fund cash needs which is disclosed in the Consolidated Statements of Cash Flows for the applicable periods. There are no material legal or functional restrictions on the use of funds from operations. Funds from operations should not be considered as an alternative to net income as an indicator of the Company's operating performance or as an alternative to cash flows as a measure of liquidity. Management considers funds from operations a supplemental measure of operating performance and along with cash flow from operating activities, financing activities and investing activities, it provides investors with an indication of the ability of the Company to incur and service debt, to make capital expenditures and to fund other cash needs. Funds from operations may not be comparable to similarly titled measures reported by other REITs since a number of REITs, including the Company, calculate funds from operations in a manner different from that used by the National Association of Real Estate Investment Trusts ("NAREIT"). Funds from operations, as defined by NAREIT, represents net income applicable to common shares before depreciation and amortization, extraordinary items and gains or losses on sales of real estate. Funds from operations as disclosed above has been modified from this definition to adjust primarily for (i) the effect of straight-lining of property rentals for rent escalations and leasing fee income and (ii) the exclusion of income arising from the amortization of below market leases net of above market leases.

⁽²⁾ Operating results for the year ended December 31, 2002, reflect the Company's January 1, 2002 acquisition of the remaining 66% of Charles E. Smith Commercial Realty L.P. ("CESCR") and the resulting consolidation of CESCR's operations. See Supplemental Information, page 33 for condensed Pro Forma Operating Results for the year ended December 31, 2001 giving effect to the CESCR acquisition as if it had occurred on January 1, 2001.

⁽³⁾ Funds from operations as previously reported for the year ended December 31, 2001 and 2000 have been revised to include income from the early extinguishment of debt of \$1,170 in 2001 and expense from the early extinguishment of debt of \$1,125 in 2000 because such items are no longer treated as extraordinary items in accordance with Generally Accepted Accounting Principles.

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MANAGEMENT'S DISCUSSION AND ANALYSIS
OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

Vornado Realty Trust

Index to Management's Discussion and Analysis
of Financial Condition and Results of Operations

Overview	4
Results of Operations:	
Years Ended December 31, 2002 and 2001	13
Years Ended December 31, 2001 and 2000	21
Supplemental Information:	
Summary of Net Income and Adjusted EBITDA for the Three Months Ended December 31, 2002 and 2001	28
Changes by segment in Adjusted EBITDA for the Three Months Ended December 31, 2002 and 2001	30
Changes by segment in Adjusted EBITDA for the Three Months Ended December 31, 2002 as compared to September 30, 2002	31
Leasing Activity	32
Pro forma Operating Results—CESCR Acquisition	33
Senior Unsecured Debt Covenant Compliance Ratios	33
Related Party Disclosure	34
Liquidity and Capital Resources:	
Cash Flows for the Years Ended December 31, 2002, 2001 and 2000	37
Funds from Operations for the Years Ended December 31, 2002 and 2001	43

Vornado Realty Trust

Overview

Management's Discussion and Analysis of Financial Condition and Results of Operations includes a discussion of the Company's consolidated financial statements for the years ended December 31, 2002, 2001 and 2000.

Operating results for the year ended December 31, 2002, reflect the Company's January 1, 2002 acquisition of the remaining 66% of Charles E. Smith Commercial Realty L.P. ("CESCR") and the resulting consolidation of CESCR's operations. See Supplemental Information, page 33, for Condensed Pro Forma Operating Results for the year ended December 31, 2001 giving effect to the CESCR acquisition as if it had occurred on January 1, 2001.

Critical Accounting Policies

In preparing the consolidated financial statements management has made estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting periods. Actual results could differ from those estimates. Set forth below is a summary of the accounting policies that management believes are critical to the preparation of the consolidated financial statements. The summary should be read in conjunction with the more complete discussion of the Company's accounting policies included in Note 2 to the consolidated financial statements in this annual report.

Real Estate

Real estate is carried at cost, net of accumulated depreciation and amortization. As of December 31, 2002, the Company's carrying amount of its real estate, net of accumulated depreciation is \$6.8 billion. Maintenance and repairs are charged to operations as incurred. Depreciation requires an estimate by management of the useful life of each property as well as an allocation of the costs associated with a property to its various components. If the Company does not allocate these costs appropriately or incorrectly estimates the useful lives of its real estate, depreciation expense may be misstated.

Upon acquisitions of real estate, the Company assesses the fair value of acquired assets (including land, buildings, tenant improvements and acquired above and below market leases and the origination cost of acquired in-place leases in accordance with SFAS No. 141) and acquired liabilities, and allocate purchase price based on these assessments. The Company assesses fair value based on estimated cash flow projections that utilize appropriate discount and capitalization rates and available market information. Estimates of future cash flows are based on a number of factors including the historical operating results, known trends, and market/economic conditions that may affect the property. The Company's properties are reviewed for impairment if events or circumstances change indicating that the carrying amount of the assets may not be recoverable. If the Company incorrectly estimates the values at acquisition or the undiscounted cash flows, initial allocations of purchase price and future impairment charges may be different. The impact of the Company's estimates in connection with acquisitions and future impairment analysis could be material to the Company's financial statements.

Notes and Mortgage Loans Receivable

The Company evaluates the collectibility of both interest and principal of each of its notes and mortgage loans receivable (\$86.6 million as of December 31, 2002) if circumstances warrant to determine whether it is impaired. If the Company fails to identify that the investee or borrower are unable to perform, the Company's bad debt expense may be different.

Partially-Owned Entities

The Company accounts for its investments in partially-owned entities (\$997.7 million as of December 31, 2002) under the equity method when the Company's ownership interest is more than 20% but less than 50% and the Company does not exercise direct or indirect control. When partially-owned investments are in partnership form, the 20% threshold may be reduced. Factors that the Company considers in determining whether or not it exercises control include substantive participating rights of partners on significant business decisions, including dispositions and acquisitions of assets, financing and operating and capital budgets, board and management representation and authority and other contractual rights of its partners. To the extent that the Company is deemed to control these entities, these entities would have to be consolidated and therefore impact the balance sheet, operations and related ratios. On a periodic basis the Company evaluates whether there are any indicators that the value of the Company's investments in partially-owned entities are impaired. An investment is impaired if management's estimate of the value of the investment is less than the carrying amount. The ultimate realization of the Company's investment in partially-owned entities is dependent on a number of factors including the performance of the investee and market conditions. If the Company determines that a decline in the value of its investee is other than temporary, then an impairment charge would be recorded.

Allowance For Doubtful Accounts

The Company periodically evaluates the collectibility of amounts due from tenants and maintains an allowance for doubtful accounts for estimated losses resulting from the inability of tenants to make required payments under the lease agreement. The Company also maintains an allowance for receivables arising from the straight-lining of rents. This receivable arises from earnings recognized in excess of amounts currently due under the lease agreements. Management exercises judgment in establishing these allowances and considers payment history and current credit status in developing these estimates. If estimates differ from actual results this would impact reported results.

Revenue Recognition

The Company has the following revenue sources and revenue recognition policies:

- **Base Rents**—income arising from tenant leases. These rents are recognized over the non-cancelable term of the related leases on a straight-line basis which includes the effects of rent steps and free rent abatements under the leases.
- **Percentage Rents**—income arising from retail tenant leases which are contingent upon the sales of the tenant exceeding a defined threshold. These rents are recognized in accordance with SAB 101, which states that this income is to be recognized only after the contingency has been removed (i.e., sales thresholds have been achieved).

Vornado Realty Trust

- Hotel Revenues—income arising from the operation of the Hotel Pennsylvania which consists of rooms revenue, food and beverage revenue, and banquet revenue. Income is recognized when rooms are occupied. Food and beverage and banquet revenue are recognized when the services have been rendered.
- Trade Show Revenues—income arising from the operation of trade shows, including rentals of booths. This revenue is recognized in accordance with the booth rental contracts when the trade shows have occurred.
- Expense Reimbursement Income—income arising from tenant leases which provide for the recovery of all or a portion of the operating expenses and real estate taxes of the respective property. This income is accrued in the same periods as the expenses are incurred.

Before the Company recognizes revenue, it assesses, among other things, its collectibility. If the Company incorrectly determines the collectibility of its revenue, its net income and assets could be overstated.

Income Taxes

The Company operates in a manner intended to enable it to continue to qualify as a Real Estate Investment Trust ("REIT") under Sections 856-860 of the Internal Revenue Code of 1986, as amended. Under those sections, a REIT which distributes at least 90% of its REIT taxable income as a dividend to its shareholders each year and which meets certain other conditions will not be taxed on that portion of its taxable income which is distributed to its shareholders. The Company intends to distribute to its shareholders 100% of its taxable income. Therefore, no provision for Federal income taxes is required. If the Company fails to distribute the required amount of income to its shareholders, it would fail to qualify as a REIT and substantial adverse tax consequences may result.

Following is a summary of Net income and Adjusted EBITDA⁽¹⁾ by segment for the years ended December 31, 2002, 2001 and 2000. Prior to 2001, income from the Company's preferred stock affiliates ("PSAs") was included in income from partially-owned entities. On January 1, 2001, the Company acquired the common stock of its PSAs and converted these entities to taxable REIT subsidiaries. Accordingly, the Hotel portion of the Hotel Pennsylvania and the management companies (which provide services to the Company's business segments and operate the Trade Show business of the Merchandise Mart division) have been consolidated effective January 1, 2001. Amounts for the year ended December 31, 2000 have been reclassified to give effect to the consolidation of these entities, as if consolidated as of January 1, 2000 (see page 10 for the details of the reclassifications by line item). In addition, the Company has revised Adjusted EBITDA as previously reported for the year ended December 31, 2001 and 2000 to include income from the early extinguishment of debt of \$1,170,000 in 2001 and expense from the early extinguishment of debt of \$1,125,000 in 2000 because such items are no longer treated as extraordinary items in accordance with Generally Accepted Accounting Principles.

December 31, 2002

(\$ in thousands)	Total	Office	Retail	Merchandise Mart	Temperature Controlled Logistics	Other ⁽²⁾
Rentals	\$1,248,903	\$ 867,938	\$127,561	\$195,899	\$ —	\$ 57,505
Expense reimbursements	159,978	89,890	51,750	14,754	—	3,584
Other income	26,189	21,221	1,653	2,951	—	364
Total revenues	1,435,070	979,049	180,964	213,604	—	61,453
Operating expenses	541,596	343,723	65,455	86,022	—	46,396
Depreciation and amortization	205,826	146,746	15,507	26,716	—	16,857
General and administrative	98,458	34,346	5,036	20,382	—	38,694
Costs of acquisitions and development not consummated	6,874	—	—	—	—	6,874
Amortization of officer's deferred compensation expense	27,500	—	—	—	—	27,500
Total expenses	880,254	524,815	85,998	133,120	—	136,321
Operating income	554,816	454,234	94,966	80,484	—	(74,868)
Income applicable to Alexander's	29,653	—	—	—	—	29,653
Income from partially-owned entities	44,458	1,966	(687)	(339)	9,707	33,811
Interest and other investment income	31,685	6,472	323	507	—	24,383
Interest and debt expense	(239,525)	(141,044)	(56,643)	(22,948)	—	(18,890)
Net (loss) gain on disposition of wholly-owned and partially-owned assets other than real estate	(17,471)	—	—	2,156	—	(19,627)
Minority interest	(140,584)	(119,910)	(13,736)	(23,910)	2,093	14,879
Income before gains on sale of real estate and cumulative effect of change in accounting principle	263,032	201,718	24,223	35,950	11,800	(10,659)
Gains on sale of real estate	—	—	—	—	—	—
Cumulative effect of change in accounting principle	(30,129)	—	—	—	(15,490)	(14,639)
Net income	232,903	201,718	24,223	35,950	(3,690)	(25,298)
Cumulative effect of change in accounting principle	30,129	—	—	—	15,490	14,639
Interest and debt expense ⁽³⁾	302,009	139,157	58,409	23,461	25,617	55,365
Depreciation and amortization ⁽³⁾	257,707	149,361	17,532	27,006	34,474	29,334
EBITDA	822,748	490,236	100,164	86,417	71,891	74,040
Adjustments:						
Minority interest	140,584	119,910	13,736	23,910	(2,093)	(14,879)
Gains (losses) on sale of real estate ⁽³⁾	(1,405)	—	—	—	2,026	(3,431)
Straight-lining of rents ⁽³⁾	(29,837)	(24,352)	(1,863)	(1,772)	—	(1,850)
Amortization of below market leases, net	(12,634)	(12,469)	(165)	—	—	—
Other	1,549	—	860	323	—	366
Adjusted EBITDA ⁽¹⁾	\$ 921,005	\$ 573,325	\$112,732	\$108,878	\$ 71,824	\$ 54,246

See Notes on page 10.

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MANAGEMENT'S DISCUSSION AND ANALYSIS
OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS *continued*

Vornado Realty Trust

December 31, 2001

(\$ in thousands)	Total	Office	Retail	Merchandise Mart	Temperature Controlled Logistics	Other ⁽²⁾
Rentals	\$ 841,999	\$461,606	\$121,023	\$197,668	\$ —	\$ 61,702
Expense reimbursements	133,114	67,470	49,436	13,801	—	2,407
Other income	10,660	3,775	1,154	3,324	—	2,407
Total revenues	985,773	532,851	171,613	214,793	—	66,516
Operating expenses	398,969	217,581	56,547	83,107	—	41,734
Depreciation and amortization	123,862	71,425	14,767	25,397	—	12,273
General and administrative	72,572	12,421	3,576	18,081	—	38,494
Costs of acquisitions not consummated	5,223	—	—	—	—	5,223
Total expenses	600,626	301,427	74,890	126,585	—	97,724
Operating income	385,147	231,424	96,723	88,208	—	(31,208)
Income applicable to Alexander's	25,718	—	—	—	—	25,718
Income from partially-owned entities	80,612	32,746	1,914	149	17,447 ⁽⁴⁾	28,356
Interest and other investment income	54,385	6,866	608	2,045	—	44,866
Interest and debt expense	(173,076)	(54,667)	(55,358)	(33,354)	—	(29,697)
Net (loss) gain on disposition of wholly-owned and partially-owned assets other than real estate	(8,070)	—	—	160	—	(8,230)
Minority interest	(112,363)	(55,932)	(16,562)	(15,650)	(10,968)	(13,251)
Income before gains on sales of real estate and cumulative effect of change in accounting principle	252,353	160,437	27,325	41,558	6,479	16,554
Gains on sale of real estate	15,495	12,445	3,050	—	—	—
Cumulative effect of change in accounting principle	(4,110)	—	—	—	—	(4,110)
Net income	263,738	172,882	30,375	41,558	6,479	12,444
Cumulative effect of change in accounting principle	4,110	—	—	—	—	4,110
Interest and debt expense ⁽³⁾	266,784	92,410	57,915	33,354	26,459	56,646
Depreciation and amortization ⁽³⁾	188,859	91,085	18,957	25,397	33,815	19,605
EBITDA	723,491	356,377	107,247	100,309	66,753	92,805
Adjustments:						
Gains on sale of real estate ⁽³⁾	(21,793)	(12,445)	(3,050)	—	—	(6,298)
Minority interest	112,363	55,932	16,562	15,650	10,968	13,251
Net gain on disposition of wholly-owned and partially-owned assets other than real estate	(160)	—	—	(160)	—	—
Straight-lining of rents ⁽³⁾	(26,134)	(20,064)	727	(4,997)	—	(1,800)
Other	(2,715)	—	(2,337)	—	716	(1,094)
Adjusted EBITDA ⁽¹⁾	\$ 785,052	\$379,800	\$119,149	\$110,802	\$ 78,437	\$ 96,864

See Notes on page 10.

December 31, 2000
(after giving effect to consolidation of PSA's—see reclassifications below)

(\$ in thousands)	Total	Office	Retail	Merchandise Mart	Temperature Controlled Logistics	Other ⁽²⁾
Rentals	\$ 788,469	\$ 406,261	\$ 129,902	\$ 171,001	\$ —	\$ 81,305
Expense reimbursements	120,074	60,767	45,490	10,654	—	3,163
Other income	17,608	5,499	2,395	4,661	—	5,053
Total revenues	926,151	472,527	177,787	186,316	—	89,521
Operating expenses	379,524	199,424	55,671	74,553	—	49,876
Depreciation and amortization	108,109	58,074	17,464	21,984	—	10,587
General and administrative	63,468	10,401	667	16,330	—	36,070
Total expenses	551,101	267,899	73,802	112,867	—	96,533
Operating income	375,050	204,628	103,985	73,449	—	(7,012)
Income applicable to Alexander's	17,363	—	—	—	—	17,363
Income from partially-owned entities	79,694	29,210	667	—	28,778 ⁽⁴⁾	21,039
Interest and other investment income	33,798	6,162	—	2,346	—	25,290
Interest and debt expense	(180,505)	(62,162)	(54,305)	(38,569)	—	(25,469)
Minority interest	(102,374)	(46,917)	(16,550)	(12,660)	(12,483)	(13,764)
Income before gains on sales of real estate	223,026	130,921	33,797	24,566	16,295	17,447
Gains on sales of real estate	10,965	8,405	2,560	—	—	—
Net income	233,991	139,326	36,357	24,566	16,295	17,447
Interest and debt expense ⁽³⁾	260,573	96,224	55,741	38,566	27,424	42,618
Depreciation and amortization ⁽³⁾	167,268	76,696	18,522	20,627	34,015	17,408
EBITDA	661,832	312,246	110,620	83,759	77,734	77,473
Adjustments:						
Minority interest	102,374	46,917	16,550	12,660	12,483	13,764
Gains on sale of real estate ⁽³⁾	(10,965)	(8,405)	(2,560)	—	—	—
Straight-lining of rents ⁽³⁾	(30,001)	(19,733)	(2,295)	(5,919)	(1,121)	(933)
Other	14,510	—	(1,654)	1,358	4,064 ⁽²⁾	10,742 ⁽³⁾
Adjusted EBITDA ⁽¹⁾	\$ 737,750	\$ 331,025	\$ 120,661	\$ 91,858	\$ 93,160	\$ 101,046

See Notes on page 10.

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MANAGEMENT'S DISCUSSION AND ANALYSIS
OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS *continued*

Vornado Realty Trust

Prior to 2001, income from the Company's investments in preferred stock affiliates ("PSAs") was included in income from partially-owned entities. On January 1, 2001, the Company acquired the common stock of its PSAs and converted these entities to taxable REIT subsidiaries. Accordingly, the operations of the Hotel portion of the Hotel Pennsylvania and the operations of the management companies (which provide services to the Company's business segments and operate the Trade Show business of the Merchandise Mart division) have been consolidated effective January 1, 2001. Amounts for the year ended December 31, 2000 have been reclassified to give effect to the consolidation of these entities, as of January 1, 2000. The effect of these reclassifications in 2000 was as follows:

(i) reduction in equity in income of partially-owned entities	\$ (8,599,000)
(ii) increase in rental revenues	64,501,000
(iii) increase in other income	8,325,000
(iv) increase in operating expenses	(41,233,000)
(v) increase in depreciation and amortization	(6,906,000)
(vi) increase in general and administrative expenses	(6,984,000)
(vii) increase in interest and debt expense	(9,104,000)
(viii) net impact	\$ —

These reclassifications had no effect on reported Net Income or Adjusted EBITDA for the year ended December 31, 2000 and no impact on any other year.

Notes:

- (1) Adjusted EBITDA represents income before interest, taxes, depreciation and amortization, extraordinary or non-recurring items, gains or losses on sales of depreciable real estate, the effect of straight-lining of rent escalations, amortization of acquired below market leases net of above market leases and minority interest. Management considers Adjusted EBITDA a supplemental measure for making decisions and assessing the performance of its segments. Adjusted EBITDA should not be considered a substitute for net income or a substitute for cash flow as a measure of liquidity. Adjusted EBITDA is presented as a measure of "operating performance" which enables the reader to identify trends from period to period and may be used to compare "same store" operating performance to other companies, as well as providing a measure for determining funds available to service debt. Adjusted EBITDA may not be comparable to similarly titled measures employed by other companies. In addition, the Company has revised Adjusted EBITDA as previously reported for the year ended December 31, 2001 and 2000 to include income from the early extinguishment of debt of \$1,170 in 2001 and expense from the early extinguishment of debt of \$1,125 in 2000 because such items are no longer treated as Extraordinary Items in accordance with Generally Accepted Accounting Principles.

(2) Adjusted EBITDA—Other is comprised of:

(amounts in thousands)	For the Year Ended December 31,		
	2002	2001	2000
Newkirk Master Limited Partnership:			
Equity in income	\$ 60,756	\$ 54,695	\$ 43,685
Interest and other income	8,795	8,700	7,300
Hotel Pennsylvania	7,636	16,978	26,866
Alexander's	34,381	19,362	18,330
Investment income and other	31,261	44,097	34,990
Corporate general and administrative expenses	(34,743)	(33,515)	(30,125)
Primestone foreclosure and impairment losses	(35,757)	—	—
Amortization of Officer's deferred compensation expense	(27,500)	—	—
Write-off of 20 Times Square pre-development costs (2002) and World Trade Center acquisition costs (2001)	(6,874)	(5,223)	—
Net gain on sale of marketable securities	12,346	—	—
Gain on transfer of mortgages	2,096	—	—
Net gain on sale of air rights.	1,688	—	—
Palisades	161	—	—
After-tax net gain on sale of Park Laurel condominium units	—	15,657	—
Write-off of net investment in Russian Tea Room	—	(7,374)	—
Write-off of investments in technology companies	—	(16,513)	—
Total	\$ 54,246	\$ 96,864	\$101,046

- (3) Interest and debt expense, depreciation and amortization, straight-lining of rents and gains on sale of real estate included in the reconciliation of net income to EBITDA or Adjusted EBITDA include amounts which are netted in income from partially-owned entities.
- (4) Excludes rent not recognized of \$19,348, \$15,281 and \$9,787 for the years ended December 31, 2002, 2001 and 2000.
- (5) Includes the reversal of \$1,266 and \$4,765 of expenses in 2001 and 2000 representing the non-cash appreciation in value of shares held in a rabbi trust in connection with a deferred compensation arrangement for the Company's President.

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MANAGEMENT'S DISCUSSION AND ANALYSIS
OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS *continued*

Vornado Realty Trust

The following table sets forth the percentage of the Company's Adjusted EBITDA by segment for the years ended December 31, 2002, 2001 and 2000. The pro forma column gives effect to the January 1, 2002 acquisition by the Company of the remaining 66% interest in CESCO described previously as if it had occurred on January 1, 2001.

	Percentage of Adjusted EBITDA			
	Year Ended December 31,			
	2002	2001	2001	2000
Office:		(Pro forma)		
New York City	33%	31%	38%	35%
CESCO	29%	26%	10%	10%
Total	62%	57%	48%	45%
Retail	12%	12%	15%	16%
Merchandise Mart Properties	12%	12%	14%	12%
Temperature Controlled Logistics	8%	8%	10%	13%
Other	6%	11%	13%	14%
	100%	100%	100%	100%

Results Of Operations

Years Ended December 31, 2002 and December 31, 2001

Revenues

The Company's revenues, which consist of property rentals, tenant expense reimbursements, hotel revenues, trade shows revenues, amortization of above and below market leases acquired under SFAS No. 141, and other income, were \$1,435,070,000 for the year ended December 31, 2002, compared to \$985,773,000 in the year ended December 31, 2001, an increase of \$449,297,000 of which \$423,128,000 resulted from the acquisition of the remaining 66% of CESCO and the resulting consolidation of its operations. Below are the details of the increase (decrease) by segment:

(amounts in thousands)

	Date of Acquisition	Total	Office	Retail	Merchandise Mart	Other
Property rentals:						
Acquisitions, dispositions and non same store revenue:						
CESCO (acquisition of remaining 66% and consolidation vs. equity method accounting for 34%)	January 2002	\$393,506	\$393,506	\$ —	\$ —	\$ —
Palisades	March 2002	4,109	—	—	—	4,109
715 Lexington Avenue	July 2001	976	—	976	—	—
Las Catalinas (acquisition of remaining 50% and consolidation vs. equity method accounting for 50%)	September 2002	3,108	—	3,108	—	—
435 Seventh Avenue (placed in service)	August 2002	2,541	—	2,541	—	—
424 Sixth Avenue	July 2002	320	—	320	—	—
Properties taken out of service for redevelopment		(767)	—	(767)	—	—
Same Store:						
Hotel activity		(7,645) ⁽¹⁾	—	—	—	(7,645) ⁽¹⁾
Trade Shows activity		(3,908) ⁽²⁾	—	—	(3,908) ⁽²⁾	—
Leasing activity ⁽³⁾		14,664	12,826	360	2,139	(661)
Total increase (decrease) in property rentals		406,904	406,332	6,538	(1,769)	(4,197)
Tenant expense reimbursements:						
Increase due to acquisitions		15,319	14,398	921	—	—
Same Store		11,545	8,022	1,393	953	1,177
Total increase (decrease) in tenant expense reimbursements		26,864	22,420	2,314	953	1,177
Other Income:						
Increase due to acquisitions		15,379	15,224	11	—	144
Same Store		150	2,222	488	(373)	(2,187)
Total increase (decrease) in other income		15,529	17,446	499	(373)	(2,043)
Total increase (decrease) in revenues		\$449,297	\$446,198	\$9,351	\$ (1,189)	\$ (5,063)

⁽¹⁾ Average occupancy and REVPAR for the Hotel Pennsylvania were 65% and \$58 for the year ended December 31, 2002 compared to 63% and \$70 for the prior year.

⁽²⁾ Reflects a decrease of \$3,580 resulting from the rescheduling of two trade shows from the fourth quarter in which they were previously held to the first quarter of 2003.

See supplemental information on page 32, for details of leasing activity and corresponding changes in occupancy.

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MANAGEMENT'S DISCUSSION AND ANALYSIS
OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS *continued*

Vornado Realty Trust

Expenses

The Company's expenses were \$880,254,000 for the year ended December 31, 2002, compared to \$600,626,000 in the year ended December 31, 2001, an increase of \$279,628,000, of which \$202,852,000 resulted from the acquisition of the remaining 66% of CESCO and the resulting consolidation of its operations. Below are the details of the increase by segment:

(amounts in thousands)	Total	Office	Retail	Merchandise Mart	Other
Operating:					
Acquisitions:					
CESCO (acquisition of remaining 66% and consolidation vs. equity method accounting for 34%)	\$ 114,438	\$ 114,438	\$ —	\$ —	\$ —
Palisades	5,158	—	—	—	5,158
715 Lexington Avenue	588	—	588	—	—
435 Seventh Avenue	198	—	198	—	—
424 Sixth Avenue	50	—	50	—	—
Las Catalinas (acquisition of remaining 50% and consolidation vs. equity method accounting for 50%)	1,341	—	1,341	—	—
Hotel activity	503	—	—	—	503
Trade Shows activity	(2,108)	—	—	(2,108) ⁽³⁾	—
Same store operations	22,459	11,704 ⁽¹⁾	6,731 ⁽²⁾	5,023 ⁽⁴⁾	(999)
	142,627	126,142	8,908	2,915	4,662
Depreciation and amortization:					
Acquisitions	71,435	67,470	1,015	—	2,950
Same store operations	10,529	7,851	(275)	1,319	1,634
	81,964	75,321	740	1,319	4,584
General and administrative:					
Acquisitions	20,944	20,944	—	—	—
Other expenses	4,942	981	1,460	2,301 ⁽⁵⁾	200
Total increase (decrease) in general and administrative	25,886	21,925	1,460	2,301	200
Amortization of officer's deferred compensation expense	27,500	—	—	—	27,500
Costs of acquisitions and development not consummated	1,651	—	—	—	1,651 ⁽⁶⁾
	\$ 279,628	\$ 223,388	\$ 11,108	\$ 6,535	\$ 38,597

⁽¹⁾ Results primarily from (i) a \$9,725 increase in insurance, security and real estate taxes, largely reimbursed by tenants, and (ii) \$2,639 for an allowance for straight-line rent receivables.

⁽²⁾ Results primarily from (i) increases in insurance costs which are reimbursed by tenants, (ii) a \$402 payment of Puerto Rico taxes related to the prior year, (iii) \$2,280 in bad debt allowances for accounts receivable and receivables arising from the straight-lining of rents in 2002 and (iv) lease termination fees and real estate tax refunds netted against expenses in 2001, which aggregated \$1,500.

⁽³⁾ Results primarily from the rescheduling of two trade shows from the fourth quarter in which they were previously held to the first quarter of 2003.

⁽⁴⁾ Reflects (i) increased insurance costs of \$1,366, (ii) a charge of \$312 from the settlement of a 1998 utility assessment, and (iii) an increase in real estate taxes of \$1,725.

⁽⁵⁾ Reflects a charge of \$954 in connection with the termination of a contract and the write-off of related deferred costs.

⁽⁶⁾ Reflects a charge in 2002 of \$6,874 for the write-off of pre-development costs at the 20 Times Square project and a charge in 2001 of \$5,223 in connection with the World Trade Center acquisition not consummated.

Income Applicable to Alexander's

Income applicable to Alexander's (loan interest income, management, leasing, development and commitment fees, and equity in income) was \$29,653,000 in the year ended December 31, 2002, compared to \$25,718,000 in the year ended December 31, 2001, an increase of \$3,935,000. This increase resulted from (i) \$6,915,000 of development and commitment fees in connection with Alexander's Lexington Avenue development project, (ii) the Company's \$3,524,000 share of Alexander's gain on sale of its Third Avenue property, partially offset by (iii) the Company's \$6,298,000 share of Alexander's gain on the sale of its Fordham Road property in the prior year.

Income from Partially-Owned Entities

In accordance with accounting principles generally accepted in the United States of America, the Company reflects the income it receives from (i) entities it owns less than 50% of and (ii) entities it owns more than 50% of, but which have a partner who has shared board and management representation and authority and substantive participating rights on all significant business decisions, on the equity method of accounting resulting in such income appearing on one line in the Company's consolidated statements of income. Following is the detail of income from partially-owned entities by investment as well as the increase (decrease) in income from partially-owned entities for the year ended December 31, 2002 as compared to the prior year:

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MANAGEMENT'S DISCUSSION AND ANALYSIS
OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS *continued*

Vornado Realty Trust

(amounts in thousands)	Total	CESCR ⁽¹⁾	Temperature Controlled Logistics	Newkirk Joint Venture	Las Catalinas Mall ⁽²⁾	Monmouth Mall ⁽³⁾	Starwood Ceruzzi Joint Venture	Partially- Owned Office Buildings	Other
Year Ended									
December 31, 2002:									
Revenues	\$ 480,363		\$ 117,663	\$ 295,369	\$ 10,671	\$ 5,760	\$ 695	\$ 50,205	
Expenses:									
Operating, general and administrative	(46,098)		(7,904)	(8,490)	(3,102)	(2,510)	(2,265)	(21,827)	
Depreciation	(106,287)		(59,328)	(34,010)	(1,482)	(943)	(1,430)	(9,094)	
Interest expense	(180,431)		(42,695)	(121,219)	(3,643)	(1,520)	—	(11,354)	
Other, net	(12,505)		(2,150)	(9,790)	(802)	48	(200)	389	
Net income/(loss)	\$ 135,042		\$ 5,586	\$ 121,860	\$ 1,642	\$ 835	\$ (3,200)	\$ 8,319	
Vornado's interest			60%	22%	50%	50%	80%	24%	
Equity in net income/(loss)	\$ 29,872		\$ 3,352	\$ 26,500	\$ 851	\$ 791 ⁽⁴⁾	\$ (2,560)	\$ 1,966	\$ (1,028)
Interest and other income	8,306		306	8,000	—	—	—	—	—
Fee income	6,280		6,049	—	—	231	—	—	—
Income from partially-owned entities	\$ 44,458	\$ — ⁽¹⁾	\$ 9,707	\$ 34,500	\$ 851	\$ 1,022	\$ (2,560)	\$ 1,966	\$ (1,028)
Year Ended									
December 31, 2001:									
Revenues	\$ 747,902	\$ 382,502	\$ 126,957	\$ 179,551	\$ 14,377		\$ 1,252	\$ 43,263	
Expenses:									
Operating, general and administrative	(180,337)	(135,133)	(8,575)	(13,630)	(2,844)		(820)	(19,335)	
Depreciation	(141,594)	(53,936)	(58,855)	(20,352)	(2,330)		(501)	(5,620)	
Interest expense	(236,996)	(112,695)	(44,988)	(65,611)	(5,705)		—	(7,997)	
Other, net	11,059	1,975	2,108	4,942	—		275	1,759	
Net income	\$ 200,034	\$ 82,713	\$ 16,647	\$ 84,900	\$ 3,498		\$ 206	\$ 12,070	
Vornado's interest		34%	60%	30%	50%		80%	34%	
Equity in net income/(loss)	\$ 67,679	\$ 28,653	\$ 9,988	\$ 25,470	\$ 1,749		\$ 165	\$ 4,093	\$ (2,439)
Interest and other income	7,579	—	2,105	5,474	—		—	—	—
Fee income	5,354	—	5,354	—	—		—	—	—
Income from partially-owned entities	\$ 80,612	\$ 28,653	\$ 17,447	\$ 30,944	\$ 1,749	\$ —	\$ 165	\$ 4,093	\$ (2,439)
(Decrease) Increase in Income from partially-owned entities	\$ (36,154)	\$ (28,653) ⁽¹⁾	\$ (7,740)	\$ 3,556	\$ (898) ⁽²⁾	\$ 1,022 ⁽³⁾	\$ (2,725) ⁽³⁾	\$ (2,127) ⁽⁶⁾	\$ 1,411 ⁽⁷⁾

⁽¹⁾ On January 1, 2002, the Company acquired the remaining 66% of CESCR it did not previously own. Accordingly, CESCR is consolidated as of January 1, 2002.

⁽²⁾ On September 20, 2002, the Company acquired the remaining 50% of the Mall and 25% of the Kmart anchor store that it did not previously own. Accordingly, Las Catalinas is consolidated for the period from September 20, 2002 to December 31, 2002.

⁽³⁾ On October 10, 2002, a joint venture, in which the Company has a 50% interest, acquired the Monmouth Mall.

⁽⁴⁾ Vornado's interest in the equity in net income of the Monmouth Mall includes a preferred return of \$748 for the year ended December 31, 2002.

⁽⁵⁾ The prior year includes \$1,394 for the Company's share of a gain on sale of a property.

⁽⁶⁾ The year ended December 31, 2002 excludes 570 Lexington Avenue which was sold in May 2001.

⁽⁷⁾ The prior year includes \$2,000 for the Company's share of equity in loss of its Russian Tea Room ("RTR") investment. In the third quarter of 2001, the Company wrote-off its entire net investment in RTR based on the operating losses and an assessment of the value of the real estate.

Interest and Other Investment Income

Interest and other investment income (interest income on mortgage loans receivable, other interest income and dividend income) was \$31,685,000 for the year ended December 31, 2002, compared to \$54,385,000 in the year ended December 31, 2001, a decrease of \$22,700,000. This decrease resulted primarily from a decrease of (i) \$12,347,000 due to the non-recognition of income on the mortgage loan to Primestone, which was foreclosed on April 30, 2002, (ii) \$4,626,000 due to a lower yield on the investment of the proceeds received from the May 2002 repayment of the Company's loan to NorthStar Partnership L.P. (22% yield in 2001) and (iii) \$2,269,000 due to the non-recognition of income on the loan to Vornado Operating.

Interest and Debt Expense

Interest and debt expense was \$239,525,000 for the year ended December 31, 2002, compared to \$173,076,000 in the year ended December 31, 2001, an increase of \$66,449,000. This increase was comprised of (i) \$100,013,000 from the acquisition of the remaining 66% of CESC and the resulting consolidation of its operations, partially offset by (ii) a \$32,035,000 savings from a 202 basis point reduction in weighted average interest rates of the Company's variable rate debt and (iii) lower average outstanding debt balances.

Net (Loss) Gain on Disposition of Wholly-owned and Partially-owned Assets Other Than Depreciable Real Estate

The following table sets forth the details of net gain on disposition of wholly-owned and partially-owned assets other than depreciable real estate for the years ended December 31, 2002 and 2001:

(amounts in thousands)	For the Year Ended December 31,	
	2002	2001
Wholly-owned Assets:		
Gain on transfer of mortgages	\$ 2,096	\$ —
Gain on sale of Kinzie Park condominiums units	2,156	—
Net gain on sale of air rights	1,688	—
Net gain on sale of marketable securities	12,346	—
Primestone foreclosure and impairment losses	(35,757)	—
Write-off of investments in technology companies	—	(16,513)
Partially-owned Assets:		
After-tax net gain on sale of Park Laurel condominium units	—	15,657
Write-off of net investment in Russian Tea Room	—	(7,374)
Other	—	160
	<hr/> \$(17,471)	<hr/> \$ (8,070)

Gain on Transfer of Mortgages

In the year ended December 31, 2002, the Company recorded a net gain of \$2,096,000 resulting from payments to the Company by third parties that assumed certain of the Company's mortgages. Under these transactions the Company paid to the third parties that assumed the Company's obligations the outstanding amounts due under the mortgages and the third parties paid the Company for the benefit of assuming the mortgages. The Company has been released by the creditors underlying these loans.

Vornado Realty Trust

Gain on Sale of Kinzie Park Condominium Units

The Company recognized a gain of \$2,156,000 during 2002, from the sale of residential condominiums in Chicago, Illinois.

Net Gain on Sale of Air Rights

The Company recognized a net gain of \$1,688,000 in the year ended December 31, 2002. See Note 3 to the consolidated financial statements in this annual report on form 10-K for further details.

Primestone Foreclosure and Impairment Losses

On September 28, 2000, the Company made a \$62,000,000 loan to Primestone Investment Partners, L.P. ("Primestone"). The Company received a 1% up-front fee and was entitled to receive certain other fees aggregating approximately 3% upon repayment of the loan. The loan bore interest at 16% per annum. Primestone defaulted on the repayment of this loan on October 25, 2001. The loan was subordinate to \$37,957,000 of other debt of the borrower that liened the Company's collateral. On October 31, 2001, the Company purchased the other debt for its face amount. The loans were secured by 7,944,893 partnership units in Prime Group Realty, L.P., the operating partnership of Prime Group Realty Trust (NYSE:PGE) and the partnership units are exchangeable for the same number of common shares of PGE. The loans are also guaranteed by affiliates of Primestone.

On November 19, 2001, the Company sold, pursuant to a participation agreement with a subsidiary of Cadim inc., a Canadian pension fund, a 50% participation in both loans at par for approximately \$50,000,000 reducing the Company's net investment in the loans at December 31, 2001 to \$56,768,000 including unpaid interest and fees of \$6,790,000. The participation did not meet the criteria for "sale accounting" under SFAS 140 because Cadim was not free to pledge or exchange the assets. Accordingly, the Company was required to account for this transaction as a borrowing secured by the loan, rather than as a sale of the loan by classifying the participation as an "Other Liability" and continuing to report the outstanding loan balance at 100% in "Notes and Mortgage Loans Receivable" on the balance sheet. Under the terms of the participation agreement, cash payments received shall be applied (i) first, to the reimbursement of reimbursable out-of-pocket costs and expenses incurred in connection with the servicing, administration or enforcement of the loans after November 19, 2001, and then to interest and fees owed to the Company through November 19, 2001, (ii) second, to the Company and Cadim, pro rata in proportion to the amount of interest and fees owed following November 19, 2001 and (iii) third, 50% to the Company and 50% to Cadim as recovery of principal.

On April 30, 2002, the Company and Cadim acquired the 7,944,893 partnership units at a foreclosure auction. The price paid for the units by application of a portion of Primestone's indebtedness to the Company and Cadim was \$8.35 per unit, the April 30, 2002 closing price of shares of PGE on the New York Stock Exchange. On June 28, 2002, pursuant to the terms of the participation agreement, the Company transferred 3,972,447 of the partnership units to Cadim.

In the second quarter, in accordance with foreclosure accounting, the Company recorded a loss on the Primestone foreclosure of \$17,671,000 calculated based on (i) the acquisition price of the units and (ii) its valuation of the amounts realizable under the guarantees by affiliates of Primestone, as compared with the net carrying amount of the investment at April 30, 2002. In the third quarter of 2002, the Company recorded a \$2,229,000 write-down on its investment based on costs expended to realize the value of the guarantees. Further, in the fourth quarter of 2002, the Company recorded a \$15,857,000 write-down of its

investment in Prime Group consisting of (i) \$14,857,000 to adjust the carrying amount of the Prime Group units to \$4.61 per unit, the closing price of PGE shares on the New York Stock Exchange at December 31, 2002 and (ii) \$1,000,000 for estimated costs to realize the value of the guarantees. The Company considered the decline in the value of the units which are convertible into stock to be other than temporary as of December 31, 2002, based on the fact that the market value of the stock has been less than its cost for more than six months, the severity of the decline, market trends, the financial condition and near-term prospects of Prime Group and other relevant factors.

At December 31, 2002, the Company's carrying amount of the investment was \$23,908,000, of which \$18,313,000 represents the carrying amount of the 3,972,447 partnership units owned by the Company (\$4.61 per unit), \$6,100,000 represents the amount expected to be realized under the guarantees, partially offset by \$1,005,000 representing the Company's share of Prime Group Realty's net loss through September 30, 2002 (see Note 4. Investments in and Advances to Partially-Owned Entities).

At February 3, 2003, the closing price of PGE shares on the New York Stock Exchange was \$5.30 per share. The ultimate realization of the Company's investment will depend upon the future performance of the Chicago real estate market and the performance of PGE, as well as the ultimate realizable value of the net assets supporting the guarantees and the Company's ability to collect under the guarantees. In addition, the Company will continue to monitor this investment to determine whether additional write-downs are required based on (i) declines in value of the shares of PGE (for which the partnership units are exchangeable) which are "other than temporary" as used in accounting literature and (ii) the amount expected to be realized under the guarantees.

Cumulative Effect of Change in Accounting Principle

Upon the adoption of SFAS No. 142—Goodwill and Other Intangible Assets, on January 1, 2002, the Company wrote off all of the goodwill associated with the Hotel Pennsylvania and the Temperature Controlled Logistics businesses aggregating \$30,129,000. This write-off was reflected as a cumulative effect of a change in accounting principle in 2002.

Minority Interest

Minority interest was \$140,584,000 for the year ended December 31, 2002 compared to \$112,363,000 for the prior year, an increase of \$28,221,000. This increase is primarily due to operating partnership units issued in connection with acquisitions.

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MANAGEMENT'S DISCUSSION AND ANALYSIS
OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS *continued*

Vornado Realty Trust

Adjusted EBITDA

Below are the details of the changes by segment in Adjusted EBITDA.

(\$ in thousands)	Total	Office	Retail	Merchandise Mart	Temperature Controlled Logistics	Other
Year ended December 31, 2001	\$785,052	\$379,800	\$119,149	\$110,802	\$78,437	\$ 96,864
2002 Operations:						
Same store operations ⁽¹⁾	1,811	18,165	(3,131) ⁽³⁾	(1,354) ⁽⁵⁾	(6,613) ⁽⁶⁾	(5,256) ⁽⁷⁾
Acquisitions, dispositions and non-recurring income and expenses	134,142	175,360	(3,286) ⁽⁴⁾	(570)	—	(37,362) ⁽⁸⁾
Year ended December 31, 2002	\$921,005	\$573,325 ⁽²⁾	\$112,732	\$108,878	\$71,824	\$ 54,246
% increase (decrease) in same store operations	.2%	4.8% ⁽²⁾	(2.6%) ⁽³⁾	(1.2%) ⁽⁵⁾	(8.4%) ⁽⁶⁾	(5.4%) ⁽⁷⁾

⁽¹⁾ Represents operations which were owned for the same period in each year and excludes non-recurring income and expenses.

⁽²⁾ Adjusted EBITDA and the same store percentage increase was \$303,368 and 5.0% for the New York City office portfolio and \$269,957 and 4.1% for the CESCO portfolio.

⁽³⁾ Primarily due to lower occupancy and increases in allowances for bad debt expense as a result of the K-Mart and other bankruptcies and the expiration of the Stop & Shop guarantees of several former Bradlees locations. Average occupancy for the year ended December 31, 2002 was 88.3% (84.0% excluding leases which have not commenced as described in the following sentences) as compared to 92% at December 31, 2001. The 88.3% occupancy rate includes leases for 490,000 square feet at five locations which have not commenced as of December 31, 2002. Three of these locations aggregating 268,000 square feet are ground leased to Lowe's which plans to demolish the existing buildings and construct its own stores at the sites and two locations containing 223,000 square feet are leased to Wal-Mart, which plans to demolish an existing building and construct its own store at one of the sites and occupy the existing store at the other site. All of these redevelopment projects are subject to governmental approvals and in some cases, the relocation of existing tenants.

⁽⁴⁾ Primarily due to the Company's share of losses from the Starwood Ceruzzi venture in 2002 of \$1,416 (before depreciation) from properties placed in service, as compared to a gain of \$1,394 from the sale of one of the venture's assets in 2001. Adjusted EBITDA aggregating \$2,600 from the acquisitions in the fourth quarter of 2002 of a 50% interest in the Monmouth Mall and the remaining 50% interest in the Las Catalinas Mall the Company did not previously own, was offset by lease termination fees and other refunds in the fourth quarter of 2001.

⁽⁵⁾ The net of a \$1,685 or 1.5% same store increase in the core portfolio and a \$3,300 or a 66% decline at the LA Mart as a result of rent reductions and increased marketing expenditures.

⁽⁶⁾ The Company reflects its 60% share of Vornado Crescent Portland Partnership's ("the Landlord") rental income it receives from AmeriCold Logistics, its tenant, which leases the underlying temperature controlled warehouses used in its business. The Company's joint venture does not recognize rental income unless earned and collection is assured or cash is received. The Company did not recognize its \$19,349 share of the rent the joint venture was due for the year ended December 31, 2002. The tenant has advised the Landlord that (i) its revenue for the year ended December 31, 2002 from the warehouses it leases from the Landlord, is lower than last year by .1%, and (ii) its gross profit before rent at these warehouses for the corresponding period decreased by \$614 (a .001% decrease). The decrease in revenue is primarily attributable to a reduction in customer inventory turns, a rate reduction with a significant customer and temporary plant shut-downs. The decrease in gross profit is primarily attributable to higher insurance and workers' compensation. In addition, the tenant's cash requirements for capital expenditures, debt service and a non-recurring pension funding were \$8,293 higher in the current year than in the prior year, which impacted the ability of the tenant to pay rent.

⁽⁷⁾ The decrease in same store operations was primarily due to (i) a \$14,973 reduction in investment income and (ii) a \$9,342 reduction in operating results at the Hotel Pennsylvania, partially offset by (iii) additional development and commitment fees from Alexander's and (iv) income from the Newkirk MLP. The reduction in investment income is primarily due to the reinvestment of the proceeds received from the repayment of the Company's \$75,000 loan to NorthStar Partnership LP. in May 2002 at lower yields (1.5% vs. 22%) and not recognizing income on the Company's foreclosed loan to Primestone and outstanding loan to Vornado Operating. The Hotel Pennsylvania's operating results reflect a reduction in average occupancy and REVPAR to 65% and \$58 for the year ended December 31, 2002, compared to 63% and \$70 for the year ended December 31, 2001.

⁽⁸⁾ Reflects net non-recurring items included in Adjusted EBITDA (see page 11 footnote 2 for details)

Years Ended December 31, 2001 and December 31, 2000

Revenues

The Company's revenues, which consist of property rentals, tenant expense reimbursements and other income, were \$985,773,000 in the year ended December 31, 2001 compared to \$926,151,000 in the prior year, an increase of \$59,622,000. These increases by segment resulted from:

(\$ in thousands)	Date of Acquisition	Total	Office	Retail	Merchandise Mart	Other
Property Rentals:						
Acquisitions:						
7 West 34th Street	November 2000	\$ 12,162	\$12,162	\$ —	\$ —	\$ —
33 North Dearborn Street	September 2000	3,928	—	—	3,928	—
L.A. Mart	October 2000	8,622	—	—	8,622	—
715 Lexington Avenue	July 2001	861	—	861	—	—
Plaza Suites on Main Street expansion	September 2001	2,784	—	—	2,784	—
Dispositions		(8,343)		(8,343) ⁽¹⁾		
Hotel Activity		(18,234)	—	—	—	(18,234) ⁽³⁾
Trade Show Activity		4,490	—	—	4,490	—
Leasing activity		47,260	43,183	(1,397) ⁽⁴⁾	6,843	(1,369) ⁽²⁾
Total increase in property rentals		53,530	55,345	(8,879)	26,667	(19,603)
Tenant expense reimbursements:						
Increase in tenant expense reimbursements due to acquisitions/dispositions		5,730	2,502	624	2,604	—
Other		7,310	4,201	3,322	543	(756)
Total increase in tenant expense reimbursements		13,040	6,703	3,946	3,147	(756)
Other income		(6,948)	(1,724)	(1,241)	(1,337)	(2,646)
Total increase in revenues		\$ 59,622	\$ 60,324	\$(6,174)	\$28,477	\$(23,005)

⁽¹⁾ Results primarily from the 14th Street and Union Square property being taken out of service for redevelopment on February 9, 2001 and the sale of the Company's Texas properties on March 2, 2000.

⁽²⁾ Results primarily from the termination of the Sports Authority lease at the Hotel Pennsylvania in January 2001.

⁽³⁾ Average occupancy and REVPAR for the Hotel Pennsylvania were 63% and \$70 for the year ended December 31, 2001 and 76% and \$87 for the year ended December 31, 2000.

⁽⁴⁾ Reflects a decrease of \$2,514 in property rentals arising from the straight-lining of rent escalations.

See Supplemental Information on page 32 for details of leasing activity.

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MANAGEMENT'S DISCUSSION AND ANALYSIS
OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS *continued*

Vornado Realty Trust

Expenses

The Company's expenses were \$600,626,000 in the year ended December 31, 2001, compared to \$551,101,000 in the prior year, an increase of \$49,525,000. This increase by segment resulted from:

(\$ in thousands)	Total	Office	Retail	Merchandise Mart	Other
Operating:					
Acquisitions, dispositions and non-recurring items	\$ 8,938	\$ 5,115	\$ (253)	\$ 6,199	\$ (2,123)
Hotel activity	(3,331)	—	—	—	(3,331) ⁽¹⁾
Same store operations	13,838	13,042	1,129	2,355	(2,688)
	19,445	18,157	876	8,554	(8,142)
Depreciation and amortization:					
Acquisitions, dispositions and non-recurring items	1,206	2,563	(2,859)	1,502	—
Hotel activity	1,121	—	—	—	1,121
Same store operations	13,426	10,788	162	1,911	565
	15,753	13,351	(2,697)	3,413	1,686
General and Administrative:					
Other expenses	8,815	2,020	2,909	1,751	2,135
Donations to Twin Towers Fund and NYC Fireman's Fund	1,250	—	—	—	1,250
Hotel activity	(1,605)	—	—	—	(1,605)
Appreciation in value of Vornado shares and other securities held in officer's deferred compensation trust	644	—	—	—	644
	9,104	2,020	2,909	1,751	2,424
Costs of acquisitions and development not consummated	5,223	—	—	—	5,223
	\$49,525	\$33,528	\$ 1,088	\$13,718	\$ 1,191

⁽¹⁾ Includes \$1,900 for the collection of a receivable from a commercial tenant of the Hotel in 2001 which was previously fully reserved.

Income Applicable to Alexander's

Income applicable to Alexander's (loan interest income, management, leasing and development fees, and equity in income) was \$25,718,000 in the year ended December 31, 2001, compared to \$17,363,000 in the prior year, an increase of \$8,355,000. This increase resulted primarily from the Company's share of Alexander's gain on sale of its Fordham Road property on January 12, 2001.

Income from Partially-Owned Entities

In accordance with generally accepted accounting principles, the Company reflects the income it receives from (i) entities it owns less than 50% of and (ii) entities it owns more than 50% of, but which have a partner who has shared board and management representation and authority and substantive participating rights on all significant business decisions, on the equity method of accounting resulting in such income appearing on one line in the Company's consolidated statements of income. Below is the detail of income from partially-owned entities by investment as well as the increase (decrease) in income from partially-owned entities for the year ended December 31, 2001 as compared to the prior year:

(\$ in thousands)	Total	CESCR	Temperature Controlled Logistics	Newkirk Joint Venture	Las Catalinas Mall	Starwood Ceruzzi Joint Venture	Partially- Owned Office Buildings	Other
Year Ended								
December 31, 2001:								
Revenues	\$ 747,902	\$ 382,502	\$ 126,957	\$ 179,551	\$ 14,377	\$ 1,252	\$ 43,263	\$ —
Expenses:								
Operating, general and administrative	(180,337)	(135,133)	(8,575)	(13,630)	(2,844)	(820)	(19,335)	—
Depreciation	(141,594)	(53,936)	(58,855)	(20,352)	(2,330)	(501)	(5,620)	—
Interest expense	(236,996)	(112,695)	(44,988)	(65,611)	(5,705)	—	(7,997)	—
Other, net	6,181	1,975	2,108	4,942	—	275	1,759	(4,878)
Net Income	\$ 195,156	\$ 82,713	\$ 16,647	\$ 84,900	\$ 3,498	\$ 206	\$ 12,070	\$ (4,878)
Vornado's interest		34%	60%	30%	50%	80%	34%	50%
Equity in net income	\$ 67,679	\$ 28,653	\$ 9,988	\$ 25,470	\$ 1,749	\$ 165	\$ 4,093	\$ (2,439)
Interest and other income	7,579	—	2,105	5,474	—	—	—	—
Fee income	5,354	—	5,354	—	—	—	—	—
Income from partially- owned entities	\$ 80,612	\$ 28,653	\$ 17,447	\$ 30,944	\$ 1,749	\$ 165	\$ 4,093	\$ (2,439)
Year Ended								
December 31, 2000:								
Revenues	\$ 698,712	\$ 344,084	\$ 154,467	\$ 143,272	\$ 14,386	\$ 303	\$ 42,200	\$ —
Expenses:								
Operating, general and administrative	(175,135)	(129,367)	(9,029)	(10,652)	(3,817)	(1,740)	(20,530)	—
Depreciation	(126,221)	(42,998)	(57,848)	(14,786)	(2,277)	(153)	(8,159)	—
Interest expense	(218,234)	(98,565)	(46,639)	(58,284)	(4,812)	—	(9,934)	—
Other, net	2,113	3,553	(3,667)	2,557	—	—	2,561	(2,891)
Net Income	\$ 181,235	\$ 76,707	\$ 37,284	\$ 62,107	\$ 3,480	\$ (1,590)	\$ 6,138	\$ (2,891)
Vornado's interest		34%	60%	30%	50%	80%	46%	98%
Equity in net income	\$ 67,392	\$ 25,724	\$ 22,370	\$ 18,632	\$ 1,817	\$ (1,150)	\$ 2,832	\$ (2,833)
Interest and other income	6,768	—	874	5,894	—	—	—	—
Fee income	5,534	—	5,534	—	—	—	—	—
Income from partially- owned entities	\$ 79,694	\$ 25,724	\$ 28,778	\$ 24,526	\$ 1,817	\$ (1,150)	\$ 2,832	\$ (2,833)
Increase (decrease) in income from partially- owned entities	\$ 918	\$ 2,929	\$ (11,331)	\$ 6,418	\$ (68)	\$ 1,315	\$ 1,261	\$ 394

Vornado Realty Trust

Interest and Other Investment Income

Interest and other investment income (interest income on mortgage loans receivable, other interest income, dividend income and net gains on marketable securities) was \$54,385,000 for the year ended December 31, 2001, compared to \$33,798,000 in the prior year, an increase of \$20,587,000. This increase resulted primarily from the acquisition of NorthStar subordinated unsecured debt (22% effective rate) on September 19, 2000 and a loan to Primestone Investment Partners, L.P. on September 28, 2000 (20% effective rate).

On September 28, 2000, the Company made a \$62,000,000 loan to Primestone Investment Partners, L.P. The Company received a 1% upfront fee and is entitled to receive certain other fees aggregating approximately 3% upon repayment of the loan. The loan bears interest at 16% per annum. Primestone Investment Partners, L.P. defaulted on the repayment of this loan on October 25, 2001. The Company's loan was subordinate to \$37,957,000 of other debt of the borrower that liened the Company's collateral. On October 31, 2001, the Company purchased the other debt for its face amount. The loans are secured by 7,944,893 partnership units in Prime Group Realty, L.P., the operating partnership of Prime Group Realty Trust (NYSE:PGE), which units are exchangeable for the same number of shares of PGE. The loans are also guaranteed by affiliates of the borrower. The Company has commenced foreclosure proceedings with respect to the collateral.

On November 19, 2001 the Company sold, pursuant to a participation agreement with a subsidiary of Cadim inc., a Canadian pension fund, a 50% participation in both loans at par for approximately \$50,000,000 reducing the Company's net investment in the loans at December 31, 2001 to \$56,768,000 including unpaid interest and fees of \$6,790,000. Under the terms of the participation agreement, cash payments received shall be applied (i) first, to the reimbursement of reimbursable out-of-pocket costs and expenses incurred in connection with the servicing, administration or enforcement of the loans after November 19, 2001, (ii) second, to the Company and Cadim pro rata in proportion to the amount of interest and fees owed to them (all of such fees and interest accrued through November 19, 2001 are for the account of Vornado and all of such fees and interest accrued after November 19, 2001 accrue on a 50/50 basis to the Company and Cadim) and (iii) third, 50% to the Company and 50% to Cadim. The Company has agreed that in the event the Company acquires the collateral in a foreclosure proceeding it will, upon the request of Cadim, deliver 50% of such collateral to Cadim.

For financial reporting at December 31, 2002, purposes, the gross amount of the loan, \$106,768,000, is included in "Notes and mortgage loans receivable" and Cadim's 50% participation, \$50,000,000, is reflected in "Other liabilities." The Company did not recognize income on these loans for the period from November 19, 2001 through December 31, 2001, and will not recognize income until such time that cash is received or foreclosure proceedings have been consummated.

Included in interest and other investment income for the year ended December 31, 2001, is \$2,422,000 of interest income from the \$31,424,000 note receivable the Company has from Vornado Operating. Vornado Operating has only one significant asset, its investment in AmeriCold Logistics and does not generate positive cash flow sufficient to cover all of its expenses. Accordingly, commencing January 1, 2002, the Company will no longer recognize the interest income due on the \$31,424,000 loan until Vornado Operating is cash flow positive in an amount sufficient to fund the interest due to the Company.

Interest and Debt Expense

Interest and debt expense was \$173,076,000 for the year ended December 31, 2001, compared to \$180,505,000 in the prior year, a decrease of \$7,429,000. This decrease resulted primarily from a \$36,270,000 savings from a 289 basis point reduction in weighted average interest rate on variable rate debt partially offset by interest on higher average outstanding loan balances. Interest and debt expense includes amortization of debt issuance costs of \$8,458,000 and \$8,423,000 for the years ended December 31, 2001 and 2000.

Net loss on disposition of wholly-owned and partially-owned assets other than depreciable real estate

The following table sets forth the details of net loss on disposition of wholly-owned and partially-owned assets other than depreciable real estate for the year ended December 31, 2001 (no gains/losses in 2000):

(\$ in thousands)

Wholly-owned Assets:

Write-off of investments in technology companies	\$(16,513)
--	------------

Partially-owned Assets:

After-tax net gain on sale of Park Laurel condominium units	15,657
Write-off of net investment in the Russian Tea Room ("RTR")	(7,374)
Other	160

\$ (8,070)

Write-off Investments in Technology Companies

In the first quarter of 2001, the Company recorded a charge of \$4,723,000 resulting from the write-off of an equity investment in a technology company. In the second quarter of 2001, the Company recorded an additional charge of \$13,561,000 resulting from the write-off of all of its remaining equity investments in technology companies due to both the deterioration of the financial condition of these companies and the lack of acceptance by the market of certain of their products and services. In the fourth quarter of 2001, the Company recorded \$1,481,000 of income resulting from the reversal of a deferred rent liability relating to the termination of an agreement permitting one of the technology companies access to its properties.

After-tax Net Gain on Sale of Park Laurel Condominium Units

In the third and fourth quarters of 2001, the Park Laurel Joint Venture (69% interest owned by the Company) completed the sale of 52 condominium units of the total 53 units and received proceeds of \$139,548,000. The Company's share of the after tax net gain was \$15,657,000 and is after a charge of \$3,953,000 (net of tax benefit of \$1,826,000) for awards accrued under the venture's incentive compensation plan.

Write-off of Net Investment in RTR

In the third quarter of 2001, the Company wrote-off its entire net investment of \$7,374,000 in RTR based on the operating losses and an assessment of the value of the real estate.

Vornado Realty Trust

Gains on Sale of Real Estate

In September 1998, Atlantic City condemned the Company's property. In the third quarter of 1998, the Company recorded a gain of \$1,694,000, which reflected the condemnation award of \$3,100,000, net of the carrying value of the property of \$1,406,000. The Company appealed the amount and on June 27, 2001, was awarded an additional \$3,050,000, which has been recorded as a gain in the quarter ended June 30, 2001.

On August 6, 2001, the Company sold its leasehold interest in 550/600 Mamaroneck Avenue for \$22,500,000, which approximated its net book value.

On May 17, 2001, the Company sold its 50% interest in 570 Lexington Avenue for \$60,000,000, resulting in a gain of \$12,445,000.

During 2000, the Company sold (i) its three shopping centers located in Texas for \$25,750,000, resulting in a gain of \$2,560,000 and (ii) its Westport, Connecticut office property for \$24,000,000, resulting in a gain of \$8,405,000.

Other

The Company recorded the cumulative effect of a change in accounting principle of \$4,110,000 in the first quarter of 2001. The Company had previously marked-to-market changes in the value of stock purchase warrants through accumulated other comprehensive loss. Under SFAS No. 133, Accounting for Derivative Instruments and Hedging Activities, as amended, those changes are recognized through earnings, and accordingly, the Company has reclassified \$4,110,000 from accumulated other comprehensive loss to the consolidated statement of income as of January 1, 2001. Future changes in value of such securities will be recorded through earnings.

Minority interest was \$112,363,000 for the year ended December 31, 2001, compared to \$102,374,000 for the prior year, an increase of \$9,989,000. This increase is primarily due to an increase in perpetual preferred units distributions for units issued in 2000 and 2001.

Adjusted EBITDA

Below are the details of the changes by segment in Adjusted EBITDA.

(\$ in thousands)	Total	Office	Retail	Merchandise Mart	Temperature Controlled Logistics	Other
Year ended December 31, 2000	\$737,750	\$331,025	\$120,661	\$ 91,858	\$ 93,160	\$101,046
2001 Operations:						
Same store operations ⁽¹⁾	32,485	37,731	3,305	7,508	(14,723) ⁽³⁾	(1,336)
Acquisitions, dispositions and non-recurring income and expenses	14,817	11,044	(4,817)	11,436	-	(2,846)
Year ended December 31, 2001	\$785,052	\$379,800 ⁽²⁾	\$119,149	\$110,802	\$ 78,437	\$ 96,864 ⁽⁴⁾
% increase (decrease) in same store operations	4.4%	11.4% ⁽²⁾	2.7%	8.2%	(15.8%) ⁽³⁾	(1.3%) ⁽⁴⁾

⁽¹⁾ Represents operations which were owned for the same period in each year.

⁽²⁾ Adjusted EBITDA and the same store percentage increase was \$295,222 and 13.7% for the New York City office portfolio and \$84,943 and 3.6% for the CESCO portfolio.

⁽³⁾ The tenant has reported that (i) its revenue for the year ended December 31, 2001 from the warehouses it leases from the Landlord, is lower than last year by 4.2% and (ii) its gross profit before rent at these warehouses for the corresponding period is lower than last year by \$26,764 (a 14.4% decline). This decrease is attributable to a reduction in total customer inventory stored at the warehouses and customer inventory turns. Based on the Landlord's policy of recognizing rental income when earned and collection is assured or cash is received, the Company did not recognize \$15,281 and \$8,606 of the rent it was due in the years ended December 31, 2001 and 2000. On December 31, 2001 the Landlord released the tenant from its obligation to pay \$39,812 of deferred rent of which the Company's share was \$23,887. This amount equals the rent which was not recognized as income by the Company and accordingly had no profit and loss effect to the Company.

⁽⁴⁾ Included in "Other" is \$2,422 of interest income from the \$31,424 note receivable the Company has from Vornado Operating. Vornado Operating has only one significant asset, its investment in AmeriCold Logistics and does not generate positive cash flow sufficient to cover all of its expenses. Accordingly, commencing January 1, 2002, the Company no longer recognizes interest income due on the \$31,424 loan until Vornado Operating is cash flow positive in an amount sufficient to fund the interest due to the Company.

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MANAGEMENT'S DISCUSSION AND ANALYSIS
OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS *continued*

Vornado Realty Trust

Supplemental Information

Three Months Ended December 31, 2002 and December 31, 2001

Below is a summary of Net Income and Adjusted EBITDA by segment for the three months ended December 31, 2002 and 2001.

(\$ in thousands)	For The Three Months Ended December 31, 2002					
	Total	Office	Retail	Merchandise Mart	Temperature Controlled Logistics	Other ⁽²⁾
Rentals	\$317,475	\$ 217,807	\$ 35,033	\$ 47,579	\$ —	\$ 17,056
Expense reimbursements	41,540	21,500	14,561	4,885	—	594
Other income	7,816	6,640	558	554	—	64
Total revenues	366,831	245,947	50,152	53,018	—	17,714
Operating expenses	144,095	89,600	19,636	21,491	—	13,368
Depreciation and amortization	55,388	39,755	4,740	6,435	—	4,458
General and administrative	26,115	7,535	1,258	5,090	—	12,232
Cost of acquisitions and development not consummated	6,874	—	—	—	—	6,874
Amortization of officer's deferred compensation expense	6,875	—	—	—	—	6,875
Total expenses	239,347	136,890	25,634	33,016	—	43,807
Operating income	127,484	109,057	24,518	20,002	—	(26,093)
Income applicable to Alexander's	7,044	—	—	—	—	7,044
Income from partially-owned entities	14,312	92	116	(119)	3,920 ⁽⁴⁾	10,303
Interest and other investment income	5,702	1,401	78	83	—	4,140
Interest and debt expense	(60,595)	(35,384)	(15,499)	(3,789)	—	(5,923)
Net loss on disposition of wholly-owned and partially-owned assets other than real estate	(16,295)	—	—	—	—	(16,295)
Minority interest	(32,773)	(30,824)	(3,661)	(7,477)	(1,558)	10,747
Net income	44,879	44,342	5,552	8,700	2,362	(16,077)
Cumulative effect of change in accounting principle	—	—	—	—	—	—
Interest and debt expense ⁽³⁾	76,861	35,079	15,499	4,022	6,223	16,038
Depreciation and amortization ⁽³⁾	69,250	41,020	5,202	6,725	8,832	7,471
EBITDA	190,990	120,441	26,253	19,447	17,417	7,432
Adjustments:						
Minority interest	32,773	30,824	3,661	7,477	1,558	(10,747)
Straight-lining of rents net of a \$4,071 allowance for uncollectible rents ⁽³⁾	(2,357)	(3,448)	481	1,065	—	(455)
Amortization of below market leases, net	(3,283)	(3,118)	(165)	—	—	—
Other	(1,454)	—	—	—	103	(1,557)
Adjusted EBITDA⁽¹⁾	\$216,669	\$ 144,699	\$ 30,230	\$ 27,989	\$19,078	\$ (5,327)

See notes on following page.

(\$ in thousands)

For The Three Months Ended December 31, 2001

	Total	Office	Retail	Merchandise Mart	Temperature Controlled Logistics	Other ⁽²⁾
Rentals	\$ 213,488	\$ 117,107	\$ 30,445	\$ 52,151	\$ —	\$ 13,785
Expense reimbursements	30,263	11,327	14,147	3,635	—	1,154
Other income	3,072	1,588	(488)	882	—	1,090
Total revenues	246,823	130,022	44,104	56,668	—	16,029
Operating expenses	99,533	52,988	15,557	20,680	—	10,308
Depreciation and amortization	32,636	18,659	4,374	7,141	—	2,462
General and administrative	20,866	3,665	263	4,795	—	12,143
Costs of acquisitions and development not consummated	223	—	—	—	—	223
Total expenses	153,258	75,312	20,194	32,616	—	25,136
Operating income	93,565	54,710	23,910	24,052	—	(9,107)
Income applicable to Alexander's	3,126	—	—	—	—	3,126
Income from partially-owned entities	18,538	8,057	(1,095)	(70)	4,538 ⁽⁴⁾	7,108
Interest and other investment income	10,454	1,100	88	268	—	8,998
Interest and debt expense	(36,633)	(10,550)	(13,983)	(7,488)	—	(4,612)
Net gain on disposition of wholly-owned and partially-owned assets other than real estate	3,719	—	—	160	—	3,559
Minority interest	(28,432)	(13,997)	(4,176)	(4,240)	(2,674)	(3,345)
Net income	64,337	39,320	4,744	12,682	1,864	5,727
Minority interest	28,432	13,997	4,176	4,240	2,674	3,345
Net gain on disposition of wholly-owned and partially-owned assets other than real estate	(160)	—	—	(160)	—	—
Interest and debt expense ⁽³⁾	64,180	20,663	14,592	7,488	6,261	15,176
Depreciation and amortization ⁽³⁾	52,386	24,012	5,066	7,141	8,604	7,563
Straight-lining of rents ⁽³⁾	(3,458)	(3,817)	1,871	(1,126)	—	(386)
Other	(3,697)	218	—	—	494	(4,409)
Adjusted EBITDA ⁽¹⁾	\$ 202,020	\$ 94,393	\$ 30,449	\$ 30,265	\$ 19,897	\$ 27,016

⁽¹⁾ Adjusted EBITDA represents EBITDA adjusted for gains or losses on sales of depreciable real estate, the effect of straight-lining of rent escalations, amortization of acquired below market leases net of above market leases and minority interest. Management considers Adjusted EBITDA a supplemental measure for making decisions and assessing the performance of its segments. Adjusted EBITDA is presented as a measure of "operating performance" which enables the reader to identify trends from period to period and may be used to compare "same store" operating performance to other companies, as well as providing a measure for determining funds available to service debt. Adjusted EBITDA may not be comparable to similarly titled measures employed by other companies.

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MANAGEMENT'S DISCUSSION AND ANALYSIS
OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS *continued*

Vornado Realty Trust

⁽²⁾ Adjusted EBITDA—Other is comprised of:

(\$ in thousands)	2002	2001
<i>Newkirk Joint Ventures (30% interest):</i>		
Equity in income of limited partnerships	\$ 14,827	\$14,238
Interest and other income	2,124	4,155
<i>Alexander's (33.1% interest)</i>	7,832	3,417
<i>Hotel Pennsylvania</i>	3,015	2,671
<i>Net gain on sale of condominium units</i>	30	1,788
<i>Corporate general and administrative expenses</i>	(11,183)	(12,143)
<i>Investment income and other</i>	6,288	12,890
<i>Primestone impairment loss</i>	(15,857)	—
<i>Officer's deferred compensation</i>	(6,875)	—
<i>Palisades</i>	1,346	—
<i>Write-off of 20 Times Square pre-development costs</i>	(6,874)	—
Total	\$ (5,327)	\$27,016

⁽³⁾ Interest and debt expense, depreciation and amortization and straight-lining of rents included in the reconciliation of net income to EBITDA or Adjusted EBITDA reflects amounts which are netted in income from partially-owned entities.

⁽⁴⁾ Net of \$6,987 and \$7,630 of rent not recognized as income for the fourth quarter of 2002 and 2001, respectively.

Below are the details of the changes by segment in Adjusted EBITDA.

(\$ in thousands)	Total	Office	Retail	Merchandise Mart	Temperature Controlled Logistics	Other
Three months ended December 31, 2001	\$202,020	\$ 94,393	\$ 30,449	\$30,265	\$19,897	\$ 27,016
2002 Operations:						
Same store operations ⁽¹⁾	(4,899)	3,558	(1,519) ⁽³⁾	(1,794) ⁽⁵⁾	(819)	(4,325) ⁽⁶⁾
Acquisitions, dispositions and non-recurring income and expenses	19,548	46,748	1,300 ⁽⁴⁾	(482)	—	(28,018) ⁽⁷⁾
Three months ended December 31, 2002	\$216,669	\$ 144,699 ⁽²⁾	\$ 30,230	\$27,989	\$19,078	\$ (5,327)
% (decrease) increase in same store operations	(2.4%)	3.8% ⁽²⁾	(5.0%) ⁽³⁾	(5.9%) ⁽⁵⁾	(4.1%)	(16.0%)

⁽¹⁾ Represents operations, which were owned for the same period in each year.

⁽²⁾ Adjusted EBITDA and same store percentage increase was \$75,303 and 3.8% for the New York City office portfolio and \$69,396 and 3.6% for the CESCO portfolio.

⁽³⁾ Primarily due to lower occupancy and increases in allowances for bad debt expense as a result of the K-Mart and other bankruptcies and the expiration of the Stop & Shop guarantees of several former Bradlees locations. Average occupancy for the quarter ended December 31, 2002 was 86%, (82% excluding leases which have not commenced) as compared to 92% at December 31, 2001.

⁽⁴⁾ Primarily due to Adjusted EBITDA aggregating \$2,600 from the acquisitions in the fourth quarter of 2002 of a 50% interest in the Monmouth Mall and the remaining 50% interest in the Las Catalinas Mall the Company did not previously own, offset by lease termination fees and other refunds in the fourth quarter of 2001.

⁽⁵⁾ Primarily due to rescheduling of two trade shows from the fourth quarter of 2002 to the first quarter of 2003.

⁽⁶⁾ Primarily due to the reinvestment of the proceeds received from the repayment of the Company's \$75,000 loan to NorthStar Partnership L.P. in May 2002 at lower yields and from not recognizing income on the Company's foreclosed loan to Primestone and loan to Vornado Operating.

⁽⁷⁾ Reflects net non-recurring items included in Adjusted EBITDA.

In comparing the financial results of the Company's segments on a quarterly basis, the following should be noted:

- The third quarter financial results of the Office and Merchandise Mart segments have historically been impacted by higher net utility costs than in each other quarter of the year;
- The fourth quarter financial results of the Retail segment have historically been higher than the first three quarters due to the recognition of percentage rental income in that quarter; and
- The second and fourth quarter financial results of the Merchandise Mart segment have historically been higher than the first and third quarters due to major trade shows occurring in those quarters.

Below are the details of the changes by segment in Adjusted EBITDA for the three months ended December 31, 2002 compared to the three months ended September 30, 2002:

(\$ in thousands)	Total	Office	Retail	Merchandise Mart	Temperature Controlled Logistics	Other
Three months ended September 30, 2002	\$ 230,599	\$ 140,248	\$ 29,277	\$ 23,424	\$ 14,864	\$ 22,786
2002 Operations:						
Same store operations ⁽¹⁾	10,537	5,851	(2,047)	3,331 ⁽²⁾	4,214 ⁽³⁾	(812)
Acquisitions, dispositions and non-recurring income and expenses	(24,467)	(1,400)	3,000	1,234	—	(27,301)
Three months ended December 31, 2002	\$ 216,669	\$ 144,699	\$ 30,230	\$ 27,989	\$ 19,078	\$ (5,327)
% increase (decrease) in same store operations	4.6%	4.2% ⁽¹⁾	(7.0%)	14.2% ⁽²⁾	28.4% ⁽³⁾	(3.6%)

⁽¹⁾ Adjusted EBITDA and same store percentage increase was \$75,303 and 6.1% for the New York City office portfolio and \$69,396 and 2.2% for the CESC portfolio.

⁽²⁾ Reflects higher income due to timing of trade shows.

⁽³⁾ Primarily due to seasonality of tenant's operations.

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MANAGEMENT'S DISCUSSION AND ANALYSIS
OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS *continued*

Vornado Realty Trust

Leasing Activity

The following table sets forth certain information for the properties the Company owns directly or indirectly, including leasing activity:

(square feet and cubic feet in thousands)	Office			Merchandise Mart		Temperature
As of December 31, 2002:	New York City	CESCR	Retail	Office	Showroom	Controlled Logistics
Square feet	14,304	13,395	12,528	2,838	5,528	17,509
Cubic feet	—	—	—	—	—	441,500
Number of properties	21	53	62	9	9	88
Occupancy rate	95.9%	93.6%	88.3%	89.2%	95.2%	78.5%
Leasing Activity:						
Quarter ended December 31, 2002:						
Square feet	138	516	890	63	121	—
Initial rent ⁽¹⁾	\$ 44.15	\$ 30.21	\$ 11.17	\$ 30.20	\$ 22.89	—
Rent per square foot on relet space:						
Square feet	124	419	776	63	121	—
Initial rent ⁽¹⁾	\$ 44.58	\$ 30.79	\$ 11.43	\$ 30.20	\$ 22.89	—
Prior escalated rent	\$ 36.10	\$ 29.22	\$ 8.67	\$ 31.85	\$ 21.68	—
Percentage increase (decrease)	23.5%	5.4%	31.8%	(5.2%)	5.6%	—
Rent per square foot on space previously vacant:						
Square feet	14	97	114	—	—	—
Initial rent ⁽¹⁾	\$ 41.94	\$ 31.01	\$ 9.46	—	—	—
Year Ended December 31, 2002:						
Square feet	579	2,342	1,960	164	911	—
Initial rent ⁽¹⁾	\$ 44.82	\$ 31.01	\$ 9.73	\$ 26.97	\$ 18.99	—
Rent per square foot on relet space:						
Square feet	457	2,025	1,339	164	911	—
Initial Rent ⁽¹⁾	\$ 44.34	\$ 31.29	\$ 12.17	\$ 26.97	\$ 18.99	—
Prior escalated rent	\$ 34.11	\$ 29.66	\$ 9.19	\$ 26.66	\$ 18.63	—
Percentage increase	30.0%	5.5%	32.4%	1.2%	2.0%	—
Tenant improvements per square foot	\$ 39.00	\$ 14.23	—	\$ 18.74	\$ 2.65	—
Leasing commissions per square foot	\$ 16.47	\$ 3.39	—	\$ 5.08	—	—
Rent per square foot on space previously vacant:						
Square feet	122	317	621 ⁽²⁾	—	—	—
Initial rent ⁽¹⁾	\$ 46.80	\$ 29.21	\$ 4.48	—	—	—
As of December 31, 2001:						
Square feet	14,300	4,386	11,301	2,841	5,532	17,695
Cubic feet	—	—	—	—	—	445,200
Number of properties	22	52	55	9	9	89
Occupancy rate	97.4%	94.8%	92.0%	89.2%	95.5%	80.7%
As of December 31, 2000:						
Square feet	14,396	4,248	11,293	2,869	5,044	17,495
Cubic feet	—	—	—	—	—	438,900
Number of properties	22	51	55	9	9	88
Occupancy rate	96.3%	97.9%	92.0%	90.2%	97.6%	82.0%

⁽¹⁾ Most leases include periodic step-ups in rent, which are not reflected in the initial rent per square foot leased.

⁽²⁾ Ground leases.

In addition to the previous, 48,000 square feet of retail space included in the NYC office properties was leased at an initial rent of \$112.01 per square foot for the year ended December 31, 2002. Further, the Company leased 140,000 square feet of garage space at a weighted average initial rent per square foot of \$19.02.

Pro Forma Operating Results — CESCO Acquisition

Below is a summary of net income, Adjusted EBITDA and funds from operations for the years ended December 31, 2002 and 2001, giving effect to the following transactions as if they had occurred on January 1, 2001: (i) the acquisition of the remaining 66% of CESCO on January 1, 2002 and (ii) the Company's November 21, 2001 sale of 9,775,000 common shares and the use of proceeds to repay indebtedness.

(Amounts in thousands, except per share amounts)	(Pro Forma)	
	Year Ended December 31,	
	2002	2001
Revenues	\$1,435,070	\$1,384,933
Net income	\$ 232,903	\$ 295,805
Preferred share dividends	(23,167)	(36,505)
Net income applicable to common shares	\$ 209,736	\$ 259,300
Net income per common share — diluted	\$ 1.91	\$ 2.55
Adjusted EBITDA	\$ 921,005	\$ 949,613
Funds from operations ⁽¹⁾	\$ 407,173	\$ 427,426
Shares used for determining funds from operations per share	112,600	109,494

⁽¹⁾ See page 43 for further details on funds from operations.

Senior Unsecured Debt Covenant Compliance Ratios

The following ratios as of and for the three months ended December 31, 2002, are computed pursuant to the covenants and definitions of the Company's senior unsecured notes due 2007.

	Actual	Required
Total Outstanding Debt/Total Assets	48%	Less than 60%
Secured Debt/Total Assets	43%	Less than 55%
Interest coverage (Annualized Combined EBITDA to Annualized Interest Expense)	2.97	Greater than 1.50
Unencumbered Assets/ Unsecured Debt	674%	Greater than 150%

The covenants and definitions of the Company's senior unsecured notes due 2007 are described in Exhibit 4.2 to the quarterly report on Form 10-Q for the three months ended September 30, 2002.

Vornado Realty Trust

Related Parties

Loan and Compensation Agreements

At December 31, 2002, the loan due from Mr. Roth, in accordance with his employment arrangement, was \$13,122,500 (\$4,704,500 of which is shown as a reduction in shareholders' equity). The loan bears interest at 4.49% per annum (based on the applicable Federal rate) and matures in January 2006. The Company also provided Mr. Roth with the right to draw up to \$15,000,000 of additional loans on a revolving basis. Each additional loan will bear interest, payable quarterly, at the applicable Federal rate on the date the loan is made and will mature on the sixth anniversary of the loan.

On May 29, 2002, Mr. Roth replaced common shares of the Company securing the Company's outstanding loan to Mr. Roth with options to purchase common shares of the Company with a value of not less than two times the loan amount. As a result of the decline in the value of the options, Mr. Roth supplemented the collateral with cash and marketable securities.

At December 31, 2002, loans due from Mr. Fascitelli, in accordance with his employment agreement, aggregated \$8,600,000. The loans, which were scheduled to mature in 2003, have been extended to 2006 in connection with the extension of Mr. Fascitelli's employment agreement (discussed below) and bear interest, payable quarterly at a weighted average interest rate of 3.97% (based on the applicable Federal rate).

Pursuant to his 1996 employment agreement, Mr. Fascitelli became entitled to a deferred payment consisting of \$5 million in cash and a convertible obligation payable November 30, 2001, at the Company's option, in either 919,540 Company common shares or the cash equivalent of their appreciated value, so long as such appreciated value is not less than \$20 million. The Company delivered 919,540 shares to a rabbi trust upon execution of the 1996 employment agreement. The Company accounted for the stock compensation as a variable arrangement in accordance with Plan B of EITF No. 97-14 "Accounting for Deferred Compensation Arrangements Where Amounts Earned Are Held in a Rabbi Trust and Invested" as the agreement permitted settlement in either cash or common shares. Following the guidance in EITF 97-14, the Company recorded changes in fair value of its compensation obligation with a corresponding increase in the liability "Officer's Deferred Compensation." Effective as of June 7, 2001, the payment date was deferred until November 30, 2004. Effective as of December 14, 2001, the payment to Mr. Fascitelli was converted into an obligation to deliver a fixed number of shares (919,540 shares), establishing a measurement date for the Company's stock compensation obligation, accordingly the Company ceased accounting for the Rabbi Trust under Plan B of the EITF and began Plan A accounting. Under Plan A, the accumulated liability representing the value of the shares on December 14, 2001, was reclassified as a component of Shareholders' Equity as "Deferred compensation shares earned but not yet delivered." In addition, future changes in the value of the shares are no longer recognized as additional compensation expense. The fair value of this obligation was \$34,207,000 at December 31, 2002. The Company has reflected this liability as Deferred Compensation Shares Not Yet Delivered in the Shareholders' Equity section of the balance sheet. For the years ended December 31, 2001 and 2000, the Company recognized approximately \$4,744,000 and \$3,733,000 of compensation expense of which \$2,612,000 and \$1,968,000 represented the appreciation in value of the shares in each period and \$2,132,000 and \$1,765,000 represented dividends paid on the shares.

Effective January 1, 2002, the Company extended its employment agreement with Mr. Fascitelli for a five-year period through December 31, 2006. Pursuant to the extended employment agreement, Mr. Fascitelli is entitled to receive a deferred payment on December 31, 2006 of 626,566 Vornado common shares

which are valued for compensation purposes at \$27,500,000 (the value of the shares on March 8, 2002, the date the extended employment agreement was executed). The shares are held in a rabbi trust for the benefit of Mr. Fascitelli and vested 100% on December 31, 2002. The extended employment agreement does not permit diversification, allows settlement of the deferred compensation obligation by delivery of these shares only, and permits the deferred delivery of these shares. The value of these shares was amortized ratably over the one-year vesting period as compensation expense.

Pursuant to the Company's annual compensation review in February 2002 with Joseph Macnow, the Company's Chief Financial Officer, the Compensation Committee approved a \$2,000,000 loan to Mr. Macnow, bearing interest at the applicable federal rate of 4.65% per annum and due January 1, 2006. The loan, which was funded on July 23, 2002, was made in conjunction with Mr. Macnow's June 2002 exercise of options to purchase 225,000 shares of the Company's common stock. The loan is collateralized by assets with a value of not less than two times the loan amount. As a result of the decline in the value of the options, Mr. Macnow supplemented the collateral with cash and marketable securities.

One other executive officer of the Company has a loan outstanding pursuant to an employment agreement totaling \$1,500,000 at December 31, 2002. The loan matures in April 2005 and bears interest at the applicable Federal rate provided (4.5% at December 31, 2002).

Transactions with Affiliates and Officers and Trustees of the Company

Alexander's

The Company owns 33.1% of Alexander's. Mr. Roth and Mr. Fascitelli are Officers and Directors of Alexander's, the Company provides various services to Alexander's in accordance with management, development and leasing agreements and the Company has made loans to Alexander's aggregating \$119,000,000 at December 31, 2002. These agreements and the loans are described in Note 4 to the Company's consolidated financial statements—Investments in Partially-Owned Entities.

The Company constructed a \$16.3 million community facility and low-income residential housing development (the "30th Street Venture"), in order to receive 163,728 square feet of transferable development rights, generally referred to as "air rights." The Company donated the building to a charitable organization. The Company sold 106,796 square feet of these air rights to third parties at an average price of \$120 per square foot. An additional 28,821 square feet of air rights was sold to Alexander's at a price of \$120 per square foot for use at Alexander's 59th Street development project (the "59th Street Project"). In each case, the Company received cash in exchange for air rights. The Company identified third-party buyers for the remaining 28,111 square feet of air rights related to the 30th Street Venture. These third-party buyers wanted to use the air rights for the development of two projects located in the general area of 86th Street, which was not within the required geographical radius of the construction site nor in the same Community Board as the low-income housing and community facility project. The 30th Street Venture asked Alexander's to sell 28,111 square feet of the air rights it already owned to the third-party buyers (who could use them) and the 30th Street Venture would replace them with 28,111 square feet of air rights. In October 2002, the Company sold 28,111 square feet of air rights to Alexander's for an aggregate sales price of \$3,059,000 (an average of \$109 per square foot). Alexander's then sold an equal amount of air rights to the third-party buyers for an aggregate sales price of \$3,339,000 (an average of \$119 per square foot).

Vornado Realty Trust

Interstate Properties

The Company manages and leases the real estate assets of Interstate Properties pursuant to a management agreement for which the Company receives an annual fee equal to 4% of base rent and percentage rent and certain other commissions. The management agreement has a term of one year and is automatically renewable unless terminated by either of the parties on sixty days' notice at the end of the term. Although the management agreement was not negotiated at arms length, the Company believes based upon comparable fees charged by other real estate companies that its terms are fair to the Company. For the years ended December 31, 2002, 2001 and 2000, \$1,450,000, \$1,655,000, and \$1,418,000 of management fees were earned by the Company pursuant to the management agreement.

Building Maintenance Service Company ("BMS")

On January 1, 2003, the Company acquired BMS, a company that provides cleaning and related services primarily to the Company's Manhattan office properties, for \$13,000,000 in cash from the estate of Bernard Mendik and certain other individuals including Mr. Greenbaum, one of the Company's executive officers. The Company paid BMS \$53,024,000, \$51,280,000, and \$47,493,000 for the years ended December 31, 2002, 2001 and 2000 for services rendered at the Company's Manhattan office properties. Although the terms and conditions of the contracts pursuant to which these services were provided were not negotiated at arm's length, the Company believes based upon comparable amounts charged to other real estate companies that the terms and conditions of the contracts were fair to the Company.

Vornado Operating Company and AmeriCold Logistics

In October 1998, Vornado Operating was spun off from the Company in order to own assets that the Company could not itself own and conduct activities that the Company could not itself conduct. The Company granted Vornado Operating a \$75,000,000 unsecured revolving credit facility which expires on December 31, 2004. Borrowings under the revolving credit facility bear interest at LIBOR plus 3%. The Company receives a commitment fee equal to 1% per annum on the average daily unused portion of the facility. No amortization is required to be paid under the revolving credit facility during its term. The revolving credit facility prohibits Vornado Operating from incurring indebtedness to third parties (other than certain purchase money debt and certain other exceptions) and prohibits Vornado Operating from paying dividends. As of December 31, 2002, \$21,989,000 was outstanding under the revolving credit facility.

Vornado Operating has disclosed that in the aggregate its investments do not, and for the foreseeable future are not expected to, generate sufficient cash flow to pay all of its debts and expenses. Further, Vornado Operating states that its only investee, AmeriCold Logistics ("Tenant"), anticipates that its Landlord, a partnership 60% owned by the Company and 40% owned by Crescent Real Estate Equities, will need to restructure the leases between the Landlord and the Tenant to provide additional cash flow to the Tenant (the Landlord has previously restructured the leases to provide additional cash flow to the Tenant). Management anticipates a further lease restructuring and the sale and/or financing of assets by AmeriCold Logistics, and accordingly, Vornado Operating is expected to have a source to repay the debt under this facility, which may be extended. Since January 1, 2002, the Company has not recognized interest income on the debt under this facility.

On December 31, 2002, the Company and Crescent Real Estate Equities formed a joint venture to acquire the Carthage, Missouri and Kansas City, Kansas quarries from AmeriCold Logistics, the Company's tenant at the cold storage warehouses (Temperature Controlled Logistics), for \$20,000,000 in cash (appraised value). The Company contributed cash of \$8,800,000 to the joint venture representing its 44% interest. AmeriCold Logistics used the proceeds from the sale to repay a portion of a loan to

Vornado Operating. Vornado Operating then repaid \$9,500,000 of the amount outstanding under the Company's revolving credit facility. On December 31, 2002, the joint venture purchased \$5,720,000 of trade receivables from AmeriCold at a 2% discount, of which the Company's share was \$2,464,000.

Other

The Company owns preferred securities in Capital Trust, Inc. ("Capital Trust") totaling \$29,212,000 at December 31, 2002. Mr. Roth, the Chairman and Chief Executive Officer of Vornado Realty Trust, is a member of the Board of Directors of Capital Trust nominated by the Company.

On May 17, 2001, the Company sold its 50% interest in 570 Lexington Avenue to the other venture partner, an entity controlled by the late Bernard Mendik, a former trustee and executive officer of the Company, for \$60,000,000, resulting in a gain to the Company of \$12,445,000. The sale was initiated by the Company's partner and was based on a competitive bidding process handled by an independent broker. The Company believes that the terms of the sale was at arm's length and were fair to the Company.

During 2002 and 2001, the Company paid approximately \$147,000 and \$136,000 for legal services to a firm in which one of the Company's trustees is a member.

On January 1, 2001, the Company acquired the common stock of various preferred stock affiliates which was owned by Officers and Trustees of the Company and converted the affiliates to taxable REIT subsidiaries. The total acquisition price was \$5,155,000. The purchase price, which was the estimated fair value, was determined by both independent appraisal and by reference to the individuals' pro rata share of the earnings of the preferred stock affiliates during the three-year period that these investments were held.

Liquidity and Capital Resources

Cash Flows for the Years Ended December 31, 2002, 2001 and 2000

Year Ended December 31, 2002

Cash and cash equivalents were \$208,200,000 at December 31, 2002, as compared to \$265,584,000 at December 31, 2001, a \$57,384,000 decrease.

Cash flow provided by operating activities of \$499,825,000 was primarily comprised of (i) income of \$232,903,000, (ii) adjustments for non-cash items of \$323,477,000, partially offset by (iii) the net change in operating assets and liabilities of \$38,239,000. The adjustments for non-cash items were comprised of (i) a cumulative effect of change in accounting principle of \$30,129,000, (ii) amortization of Officer's deferred compensation expense of \$27,500,000, (iii) depreciation and amortization of \$205,826,000, (iv) minority interest of \$140,584,000, (v) the write-off of \$6,874,000 of 20 Times Square pre-development costs, (vi) impairment losses on Primestone of \$35,757,000, partially offset by (vii) the effect of straight-lining of rental income of \$36,478,000, (viii) equity in net income of partially-owned entities and income applicable to Alexander's of \$74,111,000 and (ix) amortization of below market leases, net of \$12,634,000.

Net cash used in investing activities of \$24,117,000 was comprised of (i) recurring capital expenditures of \$52,728,000, (ii) non-recurring capital expenditures of \$42,227,000, (iii) development and redevelopment expenditures of \$63,619,000, (iv) investment in notes and mortgages receivable of \$56,935,000, (v) investments in partially-owned entities of \$100,882,000, (vi) acquisitions of real estate of \$23,665,000, (vii)

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MANAGEMENT'S DISCUSSION AND ANALYSIS
OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS *continued*

Vornado Realty Trust

cash restricted, primarily mortgage escrows of \$21,471,000 partially offset by proceeds from (viii) distributions from partially-owned entities of \$126,077,000, (ix) repayments on notes receivable of \$124,500,000 and (x) proceeds from the sale of marketable securities of \$87,896,000.

Net cash used in financing activities of \$533,092,000 was primarily comprised of (i) dividends paid on common shares of \$314,419,000, (ii) dividends paid on preferred shares of \$23,167,000, (iii) distributions to minority partners of \$146,358,000, (iv) repayments of borrowings of \$731,238,000, (v) redemption of perpetual preferred units of \$25,000,000, partially offset by proceeds from (vi) the issuance of common shares of \$56,453,000, (vii) proceeds from borrowings of \$628,335,000, of which \$499,280,000 was from the issuance of the Company's senior unsecured notes on June 24, 2002, and (viii) the exercise of employee share options of \$26,272,000.

Below are the details of capital expenditures, leasing commissions and development and redevelopment expenditures for the year ended December 31, 2002.

(Amounts in thousands)	Total	New York City Office	CESCR	Retail	Merchandise Mart	Other
Capital Expenditures:						
Expenditures to maintain the assets:						
Recurring	\$ 27,881	\$ 9,316	\$13,686	\$1,306	\$ 2,669	\$ 904
Non-recurring	35,270	6,840	16,455	—	11,975	—
	\$ 63,151	\$16,156	\$30,141	\$1,306	\$14,644	\$ 904
Tenant improvements:						
Recurring	\$ 24,847	\$12,017	\$ 5,842	\$2,309	\$ 4,679	—
Non-recurring	6,957	2,293	4,664	—	—	—
	\$ 31,804	\$14,310	\$10,506	\$2,309	\$ 4,679	—
Leasing Commissions:						
Recurring	\$ 14,345	\$ 8,854	\$ 4,416	\$ 353	\$ 614	\$ 108
Non-recurring	4,205	2,067	2,138	—	—	—
	\$ 18,550	\$10,921	\$ 6,554	\$ 353	\$ 614	\$ 108
Total Capital Expenditures and Leasing Commissions:						
Recurring	\$ 67,073	\$30,187	\$23,944	\$3,968	\$ 7,962	\$ 1,012
Non-recurring	46,432	11,200	23,257	—	11,975	—
	\$113,505	\$41,387	\$47,201	\$3,968	\$19,937	\$ 1,012
Development and Redevelopment Expenditures:						
Palisades-Fort Lee, NJ	\$ 16,750	\$ —	\$ —	\$ —	\$ —	\$16,750
640 Fifth Avenue	16,749	16,749	—	—	—	—
435 7th Avenue	12,353	12,353	—	—	—	—
Other	17,767	12,664	1,496	(596) ⁽¹⁾	1,529	2,674
	\$ 63,619	\$41,766	\$ 1,496	\$ (596)	\$ 1,529	\$19,424

⁽¹⁾ Includes reimbursements from tenants for expenditures incurred in the prior year.

Capital expenditures are categorized as follows:

Recurring—capital improvements expended to maintain a property's competitive position within the market and tenant improvements and leasing commissions for costs to re-lease expiring leases or renew or extend existing leases.

Non-recurring—capital improvements completed in the year of acquisition and the following two years which were planned at the time of acquisition and tenant improvements and leasing commissions for space which was vacant at the time of acquisition of a property.

Development and redevelopment expenditures include all hard and soft costs associated with the development or redevelopment of a property, including tenant improvements, leasing commissions and capitalized interest and operating costs until the property is substantially complete and ready for its intended use.

Acquisitions

Acquisitions of individual properties are recorded as acquisitions of real estate assets. Acquisitions of businesses are accounted for under the purchase method of accounting. The purchase price for property acquisitions and businesses acquired is allocated to acquired assets and assumed liabilities using their relative fair values as of the acquisition date based on valuations and other studies. Initial valuations are subject to change until such information is finalized no later than 12 months from the acquisition date.

Charles E. Smith Commercial Realty L.P.

On January 1, 2002, the Company completed the combination of Charles E. Smith Commercial Realty L.P. (“CESCR”) with Vornado. Prior to the combination, Vornado owned a 34% interest in CESCR. The consideration for the remaining 66% of CESCR was approximately \$1,600,000,000, consisting of 15.6 million newly issued Vornado Operating Partnership units and approximately \$1 billion of debt (66% of CESCR’s total debt). The purchase price paid by the Company was determined based on the weighted average closing price of the equity issued to CESCR unitholders for the period beginning two business days before and ending two business days after the date the acquisition was agreed to and announced on October 19, 2001. The Company also capitalized as part of the basis of the assets acquired approximately \$32,000,000 for third party acquisition related costs, including advisory, legal and other professional fees that were contemplated at the time of the acquisition. The operations of CESCR are consolidated into the accounts of the Company beginning January 1, 2002. Prior to this date the Company accounted for its 34% interest on the equity method. See page 33 for unaudited pro forma financial information for the year ended December 31, 2001.

Crystal Gateway One

On July 1, 2002, the Company acquired a 360,000 square foot office building from a limited partnership, which is approximately 50% owned by Mr. Robert H. Smith and Mr. Robert P. Kogod and members of the Smith and Kogod families, trustees of the Company, in exchange for approximately 325,700 newly issued Vornado Operating Partnership units (valued at \$13,679,000) and the assumption of \$58,500,000 of debt. The building is located in the Crystal City complex in Arlington, Virginia where the Company already owns 24 office buildings containing over 6.9 million square feet, which it acquired on January 1, 2002, in connection with the Company’s acquisition of CESCR. The operations of Crystal Gateway One are consolidated into the accounts of the Company from the date of acquisition.

Building Maintenance Service Company (“BMS”)

On January 1, 2003, the Company acquired BMS, a company which provides cleaning and related services primarily to the Company’s Manhattan office properties, for \$13,000,000 in cash from the estate of Bernard Mendik and certain other individuals including Mr. Greenbaum, one of the Company’s executive officers.

Vornado Realty Trust

Las Catalinas Mall

On September 23, 2002, the Company increased its interest in the Las Catalinas Mall located in Caguas, Puerto Rico (San Juan area) to 100% by acquiring the 50% of the mall and 25% of the Kmart anchor store it did not already own. The purchase price was \$48,000,000, including \$32,000,000 of indebtedness. The Las Catalinas Mall, which opened in 1997, contains 492,000 square feet, including a 123,000 square foot Kmart and a 138,000 square foot Sears owned by the tenant.

Monmouth Mall

On October 10, 2002, a joint venture in which the Company has a 50% interest acquired the Monmouth Mall, an enclosed super regional shopping center located in Eatontown, New Jersey containing approximately 1.5 million square feet, including four department stores, three of which aggregating 731,000 square feet are owned by the tenants. The purchase price was approximately \$164,700,000, including transaction costs of \$4,400,000. The Company made a \$7,000,000 common equity investment in the venture and provided it with \$23,500,000 of preferred equity yielding 14%. The venture financed the purchase of the Mall with \$135,000,000 of floating rate debt at LIBOR plus 2.05%, with a LIBOR floor of 2.50% on \$35,000,000, a three year term and two one-year extension options. The Company's investment in the Monmouth Mall will be accounted for under the equity method as the Company does not have unilateral control over the joint venture.

Carthage, Missouri and Kansas City, Kansas Quarries

On December 31, 2002, the Company and Crescent Real Estate Equities formed a joint venture to acquire the Carthage, Missouri and Kansas City, Kansas quarries from AmeriCold Logistics', the Company's tenant at the cold storage warehouses (Temperature Controlled Logistics) for \$20,000,000 in cash (appraised value). The Company contributed cash of \$8,800,000 to the joint venture representing its 44% interest.

The Company's future success will be affected by its ability to integrate the assets and businesses it acquires and to effectively manage those assets and businesses. The Company currently expects to continue to grow. However, its ability to do so will be dependent on a number of factors, including, among others, (a) the availability of reasonably priced assets that meet the Company's acquisition criteria and (b) the price of the Company's common shares, the rates at which the Company is able to borrow money and, more generally, the availability of financing on terms that, in the Company's view, make such acquisitions financially attractive.

Year Ended December 31, 2001

Cash flow provided by operating activities of \$387,685,000 was primarily comprised of (i) income of \$263,738,000, (ii) adjustments for non-cash items of \$131,832,000, and (iii) the net change in operating assets and liabilities of \$19,374,000. The adjustments for non-cash items were primarily comprised of (i) a cumulative effect of change in accounting principle of \$4,110,000, (ii) the write-off of the Company's remaining equity investments in technology companies of \$16,513,000, (iii) the write-off of its entire net investment of \$7,374,000 in the Russian Tea Room, (iv) depreciation and amortization of \$123,862,000, (v) minority interest of \$112,363,000, partially offset by (vi) the effect of straight-lining of rental income of \$27,230,000, and (vii) equity in net income of partially-owned entities and income applicable to Alexander's of \$106,330,000.

Net cash used in investing activities of \$79,722,000 was primarily comprised of (i) recurring capital expenditures of \$41,093,000, (ii) non-recurring capital expenditures of \$25,997,000, (iii) development and redevelopment expenditures of \$145,817,000, (iv) investment in notes and mortgages receivable of \$83,879,000, (v) investments in partially-owned entities of \$109,332,000, (vi) acquisitions of real estate of \$11,574,000, offset by, (vii) proceeds from the sale of real estate of \$162,045,000, and (viii) distributions from partially-owned entities of \$114,218,000.

Net cash used in financing activities of \$179,368,000 was primarily comprised of (i) proceeds from borrowings of \$554,115,000, (ii) proceeds from the issuance of common shares of \$377,193,000, (iii) proceeds from the issuance of preferred units of \$52,673,000, offset by, (iv) repayments of borrowings of \$835,257,000, (v) dividends paid on common shares of \$201,813,000, (vi) dividends paid on preferred shares of \$35,547,000, and (vii) distributions to minority partners of \$98,544,000.

Below are the details of capital expenditures, leasing commissions and development and redevelopment expenditures.

(\$ in thousands)	Funded by the Company					CESCR (34% Interest)
	Total	New York City Office	Retail	Merchandise Mart	Other	
Capital Expenditures:						
Expenditures to maintain the assets:						
Recurring	\$ 14,423	\$ 7,684	\$ 1,253	\$ 5,287	\$ 199	\$ 3,121
Non-recurring	20,751	13,635	—	7,116	—	6,678
	\$ 35,174	\$ 21,319	\$ 1,253	\$ 12,403	\$ 199	\$ 9,799
Tenant Improvements:						
Recurring	\$ 26,670	\$ 21,452	\$ 271	\$ 4,858	\$ 89	\$ 5,979
Non-recurring	5,246	5,246	—	—	—	190
	\$ 31,916	\$ 26,698	\$ 271	\$ 4,858	\$ 89	\$ 6,169
Leasing Commissions:						
Recurring	\$ 19,536	\$ 18,546	\$ 336	\$ 381	\$ 273	\$ 1,142
Non-recurring	7,902	7,902	—	—	—	28
	\$ 27,438	\$ 26,448	\$ 336	\$ 381	\$ 273	\$ 1,170
Total Capital Expenditures and Leasing Commissions:						
Recurring	\$ 60,629	\$ 47,682	\$ 1,860	\$ 10,526	\$ 561	\$ 10,242
Non-recurring	\$ 33,899	\$ 26,783	\$ —	\$ 7,116	\$ —	\$ 6,896
Development and Redevelopment Expenditures:						
Palisades–Fort Lee, NJ	\$ 66,173	\$ —	\$ —	\$ —	\$ 66,173	\$ —
Market Square on Main Street	29,425	—	—	29,425	—	—
Other	50,219	25,703	6,378	4,350	13,788	14,067
	\$ 145,817	\$ 25,703	\$ 6,378	\$ 33,775	\$ 79,961	\$ 14,067

Year Ended December 31, 2000

Cash flow provided by operating activities of \$249,921,000 was primarily comprised of (i) income of \$233,991,000 and (ii) adjustments for non-cash items of \$66,557,000 offset by (iii) the net change in operating assets and liabilities of \$39,102,000 and (iv) the net gain on sale of real estate of \$10,965,000. The adjustments for non-cash items were primarily comprised of (i) depreciation and amortization of \$99,846,000 and (ii) minority interest of \$102,374,000, partially offset by (iii) the effect of straight-lining

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MANAGEMENT'S DISCUSSION AND ANALYSIS
OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS *continued*

Vornado Realty Trust

of rental income of \$32,206,000 and (iv) equity in net income of partially-owned entities and income applicable to Alexander's of \$104,017,000.

Net cash used in investing activities of \$699,375,000 was primarily comprised of (i) capital expenditures of \$171,782,000, (ii) investment in notes and mortgages receivable of \$144,225,000, (iii) acquisitions of real estate of \$199,860,000, (iv) investments in partially-owned entities of \$99,974,000, (v) cash restricted of \$183,788,000, of which \$173,500,000 represents funds escrowed in connection with a mortgage financing, partially offset by (vi) proceeds from the sale of real estate of \$47,945,000 and distributions from partially-owned entities of \$68,799,000. Below are the details of acquisitions of real estate, investments in partially-owned entities, investments in notes and mortgages receivable and capital expenditures.

(\$ in thousands)	Cash	Debt Assumed	Value of Units Issued	Investment
Acquisitions of Real Estate:				
Student Housing Complex (90% Interest)	\$ 6,660	\$17,640	\$ —	\$ 24,300
33 North Dearborn Street	16,000	19,000	—	35,000
7 West 34th Street	128,000	—	—	128,000
L.A. Mart	44,000	10,000	—	54,000
Other	5,200	—	—	5,200
	\$199,860	\$46,640	\$ —	\$246,500
Investments in Partially-Owned Entities:				
Vornado Ceruzzi Joint Venture (80% interest)	\$ 21,940	\$ —	\$ —	\$ 21,940
Additional investment in Newkirk Joint Ventures	1,334	—	9,192	10,526
Loan to Alexander's	15,000	—	—	15,000
Alexander's— increase in investment to 33%	3,400	—	—	3,400
Funding of Development Expenditures:				
Fort Lee (75% interest)	10,400	—	—	10,400
Park Laurel (80% interest)	47,900	—	—	47,900
	\$ 99,974	\$ —	\$ 9,192	\$109,166
Investments in Notes and Mortgages receivable:				
Loan to NorthStar Partnership L.P.	\$ 65,000	\$ —	\$ —	\$ 65,000
Loan to Primestone Investment Partners, L.P.	62,000	—	—	62,000
Advances to Vornado Operating Company	15,251	—	—	15,251
Other	1,974	—	—	1,974
	\$144,225	\$ —	\$ —	\$144,225

Capital expenditures:	Total	New York City Office	Retail	Merchandise Mart	Other
Expenditures to maintain the assets	\$ 33,113	\$ 15,661	\$ 414	\$ 11,437	\$ 5,601
Tenant allowances	60,850	51,017	3,307	6,301	225
Total recurring capital expenditures	93,963	66,678	3,721	17,738	5,826
Redevelopment and development expenditures	63,348	40,124	3,600	19,624	—
Corporate	14,471	—	—	—	14,471
	\$171,782	\$106,802	\$ 7,321	\$ 37,362	\$ 20,297

In addition to the expenditures noted above, the Company recorded leasing commissions of \$26,133,000 in the year ended December 31, 2000, of which \$24,333,000 was attributable to New York City Office properties, \$647,000 was attributable to Retail properties and \$1,153,000 was attributable to Merchandise Mart properties.

Net cash provided by financing activities of \$473,813,000 was primarily comprised of (i) proceeds from borrowings of \$1,195,108,000, (ii) proceeds from issuance of preferred units of \$204,750,000, partially offset by, (iii) repayments of borrowings of \$633,655,000, (iv) dividends paid on common shares of \$168,688,000 (v) dividends paid on preferred shares of \$35,815,000, and (vi) distributions to minority partners of \$80,397,000.

Funds From Operations For The Years Ended December 31, 2002 And 2001

Funds from operations was \$407,173,000 in the year ended December 31, 2002, compared to \$377,693,000 in the prior year, an increase of \$29,480,000. Funds from operations includes certain items which effect comparability totaling \$41,216,000⁽¹⁾ and \$12,903,000⁽¹⁾ for the years ended December 31, 2002 and 2001. Funds from operations before these items and after minority interest was \$448,389,000 in the year ended December 31, 2002, compared to \$390,596,000 in the prior year, a \$57,793,000 increase over the prior year, or a 1.5% increase on a per share basis.

The following table reconciles funds from operations and net income:

(\$ in thousands)	For the Year Ended December 31,	
	2002	2001
Net income applicable to common shares	\$209,736	\$227,233
Cumulative effect of a change in accounting principle	30,129	4,110
Depreciation and amortization of real property	195,808	119,568
Straight-lining of property rentals for rent escalations, net of a \$4,071 allowance in 2002	(27,295)	(24,314)
Amortization of below market leases, net	(12,634)	—
Leasing fees received in excess of income recognized	1,318	1,954
Appreciation of securities held in officer's deferred compensation trust	—	3,023
Net gain on sale of 570 Lexington Avenue through a partially-owned entity	—	(12,445)
Net gain from condemnation proceeding	—	(3,050)
Proportionate share of adjustments to equity in net income of partially-owned entities to arrive at funds from operations:		
Depreciation and amortization of real property	51,881	65,588
Net gain on sales of real estate	(3,431)	(6,298)
Other	835	(371)
Minority interest in excess of preferential distributions	(45,324)	(16,810)
	401,023	358,188
Series A preferred shares	6,150	19,505
Funds from operations — diluted ⁽²⁾	\$407,173	\$377,693

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MANAGEMENT'S DISCUSSION AND ANALYSIS
OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS *continued*

Vornado Realty Trust

The number of shares used for determining funds from operations per share is as follows:

(in thousands)	For the Year Ended December 31,	
	2002	2001
Weighted average shares used for determining diluted income per share	109,669	92,073
Series A preferred shares	2,931	7,646
Shares used for determining diluted funds from operations per share ⁽²⁾	112,600	99,719

Funds from operations does not represent cash generated from operating activities in accordance with accounting principles generally accepted in the United States of America and is not necessarily indicative of cash available to fund cash needs which is disclosed in the Consolidated Statements of Cash Flows for the applicable periods. There are no material legal or functional restrictions on the use of funds from operations. Funds from operations should not be considered as an alternative to net income as an indicator of the Company's operating performance or as an alternative to cash flows as a measure of liquidity. Management considers funds from operations a supplemental measure of operating performance and along with cash flow from operating activities, financing activities and investing activities, it provides investors with an indication of the ability of the Company to incur and service debt, to make capital expenditures and to fund other cash needs. Funds from operations may not be comparable to similarly titled measures reported by other REITs since a number of REITs, including the Company, calculate funds from operations in a manner different from that used by NAREIT. Funds from operations, as defined by NAREIT, represents net income applicable to common shares before depreciation and amortization, extraordinary items and gains or losses on sales of real estate. Funds from operations as disclosed above has been modified from this definition to adjust primarily for the (i) effect of straight-lining of property rentals for rent escalations and leasing fee income and (ii) the exclusion of income arising from the amortization of acquired below market leases, net of above market leases.

⁽¹⁾ *Certain items which affect comparability included in funds from operations above are as follows:*

	For the Year Ended December 31,	
	2002	2001
Primestone foreclosure and impairment losses	\$(35,757)	\$ —
Amortization of officer's deferred compensation	(27,500)	—
Gains on sale of marketable securities	12,346	—
Gain on sale of residential condominium units	2,156	15,657
Gains on transfer of mortgages	2,096	—
Gains on sale of air rights	1,688	—
Write-off of investments in technology companies	—	(16,513)
Write-off of net investment in Russian Tea Room	—	(7,374)
Donations to Twin Towers and NYC Fireman's Funds	—	(1,250)
Write-off of 20 Times Square pre-development costs (2002) and World Trade Center acquisition costs (2001)	(6,874)	(5,223)
Minority interest	10,629	1,800
	\$(41,216)	\$(12,903)

⁽²⁾ *Assuming all of the convertible units of the Operating Partnership were converted to shares, the minority interest in partnership earnings would not be deducted in calculating funds from operations and the shares used in calculating funds from operations per share would be increased to reflect the conversion. Funds from operations per share would not change. The following table reconciles funds from operations as shown above, to the Operating Partnership's funds from operations for the years ended December 31, 2002 and 2001:*

(\$ in thousands)	For the Year Ended December 31,	
	2002	2001
Funds from operations, as above	\$407,173	\$ 377,693
Addback of minority interest reflected as equity in the Operating Partnership	105,001	52,678
Operating Partnership funds from operations	\$512,174	\$ 430,371

The number of shares to be used for determining Operating Partnership funds from operations per share is as follows:

(Shares/units in thousands)		
Shares used for determining diluted funds from operations per share, as above	112,600	99,719
Convertible units:		
Non-Vornado owned Class A units	21,269	6,140
Class D units	—	—
B-1 units	822	822
B-2 units	411	411
C-1 units	855	855
E-1 units	5,680	5,680
Shares used for determining Operating Partnership diluted funds from operations per share	141,637	113,627

Below are the cash flows provided by (used in) operating, investing and financing activities:

(\$ in thousands)	For the Year Ended December 31,	
	2002	2001
Operating activities	\$ 499,825	\$ 387,685
Investing activities	\$ (24,117)	\$ (79,722)
Financing activities	\$ (533,092)	\$ (179,368)

Certain Future Cash Requirements

For 2003, the Company has budgeted approximately \$197.3 million for capital expenditures (excluding acquisitions) and leasing commissions as follows:

(\$ and square feet in thousands)	Total	New York Office	CESCR Office	Temperature			Other
				Merchandise Retail	Controlled Mart	Logistics	
Expenditures to maintain the assets	\$ 71,900	\$23,100	\$21,800	\$ —	\$20,200	\$5,700 ⁽¹⁾	\$1,100 ⁽²⁾
Tenant improvements	\$ 98,195	\$32,500	\$40,300	\$5,095	\$20,300	\$ —	\$ —
Per square foot		\$ 38.33	\$ 16.36	\$ 7.34	\$ 15.32		
Leasing Commissions	\$ 27,221	\$15,000	\$ 9,100	\$ 821	\$ 2,300		
Per square foot		\$ 17.69	\$ 3.69	—	\$ 1.74		
Total Capital Expenditures and Leasing Commissions	\$197,316	\$70,600	\$71,200	\$5,916	\$42,800	\$5,700	\$1,100
Square feet leased		848	2,463	694	1,325		

⁽¹⁾ Represents the Company's 60% share of the Vornado Crescent Portland Partnership's obligation to fund \$9,500 of capital expenditures per annum.

⁽²⁾ Primarily for the Hotel Pennsylvania.

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MANAGEMENT'S DISCUSSION AND ANALYSIS
OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS *continued*

Vornado Realty Trust

In addition to the capital expenditures reflected above, the Company is currently engaged in certain development and redevelopment projects for which it has budgeted approximately \$230.9 million to be expended as follows:

(\$ in millions)	Actual/ Estimated Completion Date	The Company's Share of		
		Actual/ Estimated Project Cost	Costs Expended in Year Ended December 31, 2002	Estimated Costs to Complete
Completed in 2002:				
Office:				
GreenPoint site adjacent to One Penn Plaza— redevelopment of 28,000 square feet of retail space	Spring 2002	\$ 10.6	\$ 5.5	
175 Lexington Avenue—construction of a 45,000 square foot building containing approximately 41,000 square feet of low income residential housing exchanged for 163,728 square feet of air rights	Summer 2002	16.3	7.2	
Retail:				
435 Seventh Avenue—demolition of existing buildings and the construction of 43,000 square feet of retail space leased to Hennes & Mauritz	Fall 2002	21.7	15.0	
Merchandise Mart:				
Wells Kinzie Garage—Chicago (50% interest)— 244,000 square foot parking garage (746 parking spaces) adjacent to 400 North LaSalle	Spring 2002	11.1	4.1	
Other:				
Fort Lee, New Jersey (95% interest)— construction of a 41-story, 855,000 square foot high rise rental apartment complex containing 538 apartments	Spring 2002	126.9	12.2	
		\$186.6	\$44.0	
In Process:				
Office:				
New York City:				
640 Fifth Avenue—construction of additional 47,000 square feet of office space and redevelopment of existing building	Fall 2003	\$ 60.6	\$ 16.8	\$ 43.8
CESCR:				
Crystal City—construction of additional 57,000 square feet of retail space	Fall 2004	42.0	2.2	39.8
Retail:				
4 Union Square South—redevelopment of 230,000 square foot building of which 48,000 square feet is leased to Whole Foods and 26,000 square feet is leased to Forever 21	Fall 2003	46.0	2.4	43.6
Merchandise Mart:				
400 North LaSalle, Chicago (85% interest)— construction of 378,000 square foot high rise rental apartment complex containing 453 apartments	Fall 2003	77.3	37.6	39.7
Other:				
Penn Plaza Signage District—erection of up to 21 signs at various locations in the Penn Plaza District	Spring 2005	28.0	2.4	24.0
		\$253.9	\$61.4	\$190.9

In addition to the projects noted above, the Company is in the process of redeveloping fifteen of its shopping centers, seven of which include locations previously leased to Bradlees. The total cost of this redevelopment program, which includes the demolition of existing buildings, site work and tenant improvements, is estimated to be approximately \$40 million. The Company is also in the pre-development phase of a number of projects including: (i) retail space in the Penn Plaza area and at 715 Lexington Avenue, (ii) repositioning of the Hotel Pennsylvania and (iii) expansions of the Green Acres and Monmouth malls. There can be no assurance that any of the above projects will be ultimately completed, completed on time or completed for the budgeted amount.

No cash requirements have been budgeted for the capital expenditures and amortization of debt of Alexander's, The Newkirk MLP, or any other entity that is partially owned by the Company. These investees are expected to fund their own cash requirements.

Financing Activities and Contractual Obligations

Below is a schedule of the Company's contractual obligations and commitments at December 31, 2002:

(\$ in thousands)	Total	1 Year	2-3 Years	4-5 Years	Thereafter
Contractual Cash Obligations:					
Mortgages and Notes Payable	\$3,537,720 ⁽¹⁾	\$449,526 ⁽¹⁾	\$705,589	\$ 550,321	\$1,832,284
Senior Unsecured Notes due 2007	533,600	—	—	533,600	—
Unsecured Revolving Credit Facility	—	—	—	—	—
Operating Leases	1,029,171	15,347	29,285	29,559	954,980
Total Contractual Cash Obligations	\$5,100,491	\$464,873	\$734,874	\$1,113,480	\$2,787,264
Commitments:					
Standby Letters of Credit	\$ 16,779	\$ 16,779	\$ —	\$ —	\$ —
Other Guarantees	—	—	—	—	—
Total Commitments	\$ 16,779	\$ 16,779	\$ —	\$ —	\$ —

⁽¹⁾ Includes \$153,659, which is offset by an equivalent amount of cash held in a restricted mortgage escrow account.

The Company is reviewing various alternatives for the repayment or refinancing of debt coming due during 2003. The Company has \$1 billion available under its revolving credit facility which matures in July 2003 and a number of properties which are unencumbered.

The Company's credit facility contains customary conditions precedent to borrowing such as the bring down of customary representations and warranties as well as compliance with financial covenants such as minimum interest coverage and maximum debt to market capitalization. The facility provides for higher interest rates in the event of a decline in the Company's ratings below Baa3/BBB. This facility also contains customary events of default which could give rise to acceleration and include such items as failure to pay interest or principal and breaches of financial covenants such as maintenance of minimum capitalization and minimum interest coverage.

Vornado Realty Trust

The Company carries comprehensive liability and all risk property insurance (fire, flood, extended coverage and rental loss insurance) with respect to its assets. The Company's all risk insurance policies in effect before September 11, 2001 do not expressly exclude coverage for hostile acts, except for acts of war. Since September 11, 2001, insurance companies have for the most part excluded terrorist acts from coverage in all risk policies. The Company has generally been unable to obtain all risk insurance which includes coverage for terrorist acts for policies it has renewed since September 11, 2001, for each of its businesses. In 2002, the Company obtained \$200,000,000 of separate coverage for terrorist acts for each of its New York City Office, Washington, D.C. Office, Retail and Merchandise Mart businesses and \$60,000,000 for its Temperature Controlled Logistics business. Therefore, the Company is at risk for financial loss in excess of these limits for terrorist acts (as defined), which loss could be material.

The Company's debt instruments, consisting of mortgage loans secured by its properties (which are generally non-recourse to the Company), its senior unsecured notes due 2007 and its revolving credit agreement, contain customary covenants requiring the Company to maintain insurance. There can be no assurance that the lenders under these instruments will not take the position that an exclusion from all risk insurance coverage for losses due to terrorist acts is a breach of these debt instruments that allows the lenders to declare an event of default and accelerate repayment of debt. The Company has received correspondence from four lenders regarding terrorism insurance coverage, which the Company has responded to. In these letters the lenders took the position that under the agreements governing the loans provided by these lenders the Company was required to maintain terrorism insurance on the properties securing the various loans. The aggregate amount of borrowings under these loans as of December 31, 2002 was approximately \$770.4 million, and there was no additional borrowing capacity. Subsequently, the Company obtained an aggregate of \$360 million of separate coverage for "terrorist acts." To date, one of the lenders has acknowledged to the Company that it will not raise any further questions based on the Company's terrorism insurance coverage in place, and the other three lenders have not raised any further questions regarding the Company's insurance coverage. If lenders insist on greater coverage for these risks, it could adversely affect the Company's ability to finance and/or refinance its properties and to expand its portfolio.

On November 26, 2002, the Terrorism Risk Insurance Act of 2002 was signed into law. Under this new legislation, through 2004 (with a possible extension through 2005), regulated insurers must offer coverage in their commercial property and casualty policies (including existing policies) for losses resulting from defined "acts of terrorism." The Company cannot currently anticipate whether the scope and cost of such coverage will be commercially reasonable. As a result of the legislation, in February 2003 the Company obtained \$300 million of per occurrence coverage for terrorist acts for its New York City Office, Washington, D.C. Office and Merchandise Mart businesses, of which \$240 million is for Certified Acts, as defined in the legislation. The Company maintains \$200 million and \$60 million of separate aggregate coverage that it had in 2002 for each of its Retail and Temperature Controlled Logistics businesses (which has been renewed as of January 1, 2003). The Company's current Retail property insurance carrier has advised the Company that there will be an additional premium of approximately \$11,000 per month through the end of the policy term (June 30, 2003) for "Acts of Terrorism" coverage, as defined in the new legislation and that the situation may change upon renewal.

In addition, many of the Company's non-recourse mortgages contain debt service covenants which if not satisfied could require cash collateral. These covenants are not "ratings" related.

In conjunction with the closing of Alexander's Lexington Avenue construction loan on July 3, 2002, the Company agreed to guarantee, among other things, the lien free, timely completion of the construction

of the project and funding of all project costs in excess of a stated budget, as defined in the loan agreement, if not funded by Alexander's.

Corporate

On June 24, 2002, the Company completed an offering of \$500,000,000 aggregate principal amount of 5.625% senior unsecured notes due June 15, 2007. Interest on the notes is payable semi-annually on June 15th and December 15th, commencing December 15, 2002. The net proceeds of approximately \$496,300,000 were used to repay the mortgages on 350 North Orleans, Two Park Avenue, the Merchandise Mart and Seven Skyline. On June 27, 2002, the Company entered into interest rate swaps that effectively converted the interest rate on the \$500,000,000 senior unsecured notes due 2007 from a fixed rate of 5.625% to a floating rate of LIBOR plus .7725%, based upon the trailing 3-month LIBOR rate (2.5% if set on December 31, 2002).

On February 25, 2002, the Company sold 884,543 common shares to a closed-end fund and 514,200 shares to a unit investment trust based on the closing price of \$42.96 on the NYSE. The net proceeds to the Company were approximately \$57,042,000.

The Company has an effective shelf registration under which the Company can offer an aggregate of approximately \$895,479,000 of equity securities and Vornado Realty L.P. can offer an aggregate of \$500,720,000 of debt securities.

The Company anticipates that cash from continuing operations will be adequate to fund business operations and the payment of dividends and distributions on an on-going basis for more than the next twelve months; however, capital outlays for significant acquisitions will require funding from borrowings or equity offerings.

Recently Issued Accounting Standards

SFAS No. 141 — Business Combinations

SFAS No. 141 — Business Combinations requires companies to account for the value of leases acquired and the costs of acquiring such leases separately from the value of the real estate for all acquisitions subsequent to July 1, 2001. Accordingly, the Company has evaluated the leases in place for (i) the remaining 66% of CESCO it did not previously own which it acquired on January 1, 2002, (ii) the remaining 50% of the Las Catalinas Mall it did not previously own which it acquired on September 23, 2002 and (iii) a 50% interest in the Monmouth Mall which it acquired on October 10, 2002; to determine whether they were acquired at market, above market or below market. The Company's evaluations were based on (i) the differences between contractual rentals and the estimated market rents over the applicable lease term discounted back to the date of acquisition utilizing a discount rate adjusted for the credit risk associated with the respective tenants and (ii) the estimated cost of acquiring such leases giving effect to the Company's history of providing tenant improvements and paying leasing commissions.

As a result of its evaluations, as of December 31, 2002, the Company has recorded a deferred credit of \$48,430,000 representing the value of acquired below market leases, deferred charges of \$15,976,000, for the value of acquired above market leases and \$3,621,000 for origination costs. In addition, in the year ended December 31, 2002 the Company has recognized property rentals of \$12,634,000 for the amortization of below market leases net of above market leases, and depreciation expense of \$1,214,000 for the

Vornado Realty Trust

amortization of the lease origination costs and additional building depreciation resulting from the reallocation of the purchase price of the applicable properties.

SFAS No. 142— Goodwill and Other Intangible Assets

In June 2001, the Financial Accounting Standards Board (“FASB”) issued Statement of Financial Accounting Standards (“SFAS”) No. 142, Goodwill and Other Intangible Assets (effective January 1, 2002). SFAS No. 142 specifies that goodwill and some intangible assets will no longer be amortized but instead be subject to periodic impairment testing. SFAS No. 142 provides specific guidance for impairment testing of these assets and removes them from the scope of SFAS No. 121, Accounting for the Impairment of Long-Lived Assets. The Company’s goodwill balance on December 31, 2001 of \$30,129,000 consisted of \$14,639,000 related to the Hotel Pennsylvania acquisition and \$15,490,000 related to the acquisition of the Temperature Controlled Logistics businesses.

Prior to January 1, 2002, the Company performed impairment testing in accordance with SFAS 121. The Company reviewed for impairment whenever events or changes in circumstances indicated that the carrying amount of an asset may not be recoverable. Given the decrease in the estimated market values and the deteriorating performance of Hotel Pennsylvania and Temperature Controlled Logistics, the Company performed a review for recoverability estimating the future cash flows expected to result from the use of the assets and their eventual disposition. As of December 31, 2001, the sum of the expected cash flows (undiscounted and without interest charges) exceeded the carrying amounts of goodwill, and therefore no impairments were recognized.

Upon adoption of SFAS 142 on January 1, 2002, the Company tested the goodwill for impairment at the reporting level unit utilizing the prescribed two-step method. The first step compared the fair value of the reporting unit (determined based on a discounted cash flow approach) with its carrying amount. As the carrying amount of the reporting unit exceeded its fair value, the second step of the impairment test was performed to measure the impairment loss. The second step compared the implied fair value of goodwill with the carrying amount of the goodwill. As the carrying amounts of the goodwill exceeded the fair values, on January 1, 2002 the Company wrote-off all of the goodwill of the Hotel and the Temperature Controlled Logistics business as an impairment loss totaling \$30,129,000. The write-off has been reflected as a cumulative effect of change in accounting principle on the income statement. Earnings allocable to the minority interest has been reduced by their pro-rata share of the write-off of goodwill.

Previously reported “Income before gains on sale of real estate and cumulative effect of change in accounting principle” and “Net income applicable to common shares” for the year ended December 31, 2001 would have been approximately \$972,000 higher, or \$2.35 and \$2.48 per diluted share, if such goodwill was not amortized in the prior year.

SFAS No. 143— Accounting for Asset Retirement Obligations and SFAS No. 144— Accounting for the Impairment or Disposal of Long-Lived Assets

In August 2001, the FASB issued SFAS No. 143, Accounting for Asset Retirement Obligations (effective January 1, 2003) and SFAS No. 144, Accounting for the Impairment or Disposal of Long-Lived Assets (effective January 1, 2002). SFAS No. 143 requires the recording of the fair value of a liability for an asset retirement obligation in the period which it is incurred. SFAS No. 144 supersedes current accounting literature and now provides for a single accounting model for long-lived assets to be disposed of by sale and requires discontinued operations presentation for disposals of a “component” of an entity. The adoption

of these statements did not have a material effect on the Company's financial statements; however under SFAS No. 144, if the Company were to dispose of a material operating property, such property's results of operations will have to be separately disclosed as discontinued operations in the Company's financial statements.

SFAS No. 145—Rescission of SFAS No. 4, 44, and 64, Amendment of SFAS No. 13, and Technical Corrections

In April 2002, the FASB issued SFAS No. 145, Rescission of SFAS No. 4, 44, and 64, Amendment of SFAS No. 13, and Technical Corrections. SFAS No. 145 requires, among other things, (i) that the modification of a lease that results in a change of the classification of the lease from capital to operating under the provisions of SFAS No. 13 be accounted for as a sale-leaseback transaction and (ii) the reporting of gains or losses from the early extinguishment of debt as extraordinary items only if they met the criteria of Accounting Principles Board Opinion No. 30, Reporting the Results of Operations. The rescission of SFAS No. 4 is effective January 1, 2003. The amendment of SFAS No. 13 is effective for transactions occurring on or after May 15, 2002. The adoption of this statement did not have a material effect on the Company's financial statements.

SFAS No. 146—Accounting for Costs Associated with Exit or Disposal Activities

In July 2002, the FASB issued SFAS No. 146, Accounting for Costs Associated with Exit or Disposal Activities (effective January 1, 2003). SFAS No. 146 replaces current accounting literature and requires the recognition of costs associated with exit or disposal activities when they are incurred rather than at the date of a commitment to an exit or disposal plan. The Company does not anticipate that the adoption of this statement will have a material effect on the Company's financial statements.

SFAS No. 148—Accounting for Stock-Based Compensation—Transition and Disclosure—An Amendment of FASB Statement No. 123

On August 7, 2002, the Company announced that beginning January 1, 2003, it will expense the cost of employee stock options in accordance with the SFAS No. 123, Accounting For Stock-Based Compensation. In December 2002, the FASB issued SFAS No. 148—Accounting for Stock-Based Compensation—Transition and Disclosure—An Amendment of FASB Statement No. 123 to amend the transition and disclosure provisions of SFAS No. 123. Specifically, SFAS No. 123, as amended, would permit two additional transition methods for entities that adopt the fair value method of accounting for stock based employee compensation. The Company will adopt SFAS No. 123 prospectively by valuing and accounting for employee stock options granted in 2003 and thereafter. The Company will utilize a binomial valuation model and appropriate market assumptions to determine the value of each grant. Stock-based compensation expense will be recognized on a straight-line basis over the vesting period of the respective grants.

FASB Interpretation No. 45—Guarantor's Accounting and Disclosure Requirements for Guarantees, Including Indirect Guarantees of Indebtedness of Others.

In November 2002, the FASB issued Interpretation No. 45—Guarantor's Accounting and Disclosure Requirements for Guarantees, Including Indirect Guarantees of Indebtedness of Others, which elaborates on the disclosures to be made by a guarantor in its interim and annual financial statements about its obligations under certain guarantees that it has issued. The initial recognition and measurement provisions of this Interpretation are applicable on a prospective basis to guarantees issued or modified after December 31, 2002. The Company believes that the adoption of this interpretation will not have a material effect to the Company's financial statements.

Vornado Realty Trust

FASB Interpretation No. 46—Consolidation of Variable Interest Entities

In January 2003, the FASB issued Interpretation No. 46—Consolidation of Variable Interest Entities, which requires the consolidation of an entity by an enterprise (i) if that enterprise, known as a “primary beneficiary,” has a variable interest that will absorb a majority of the entity’s expected losses if they occur, receive a majority of the entity’s expected residual returns if they occur, or both and (ii) if the entity is a variable interest entity, as defined by Interpretation No. 46. An entity is a variable interest entity if (a) the total equity investment at risk in the entity is not sufficient to permit the entity to finance its activities without additional subordinated financial support from other parties or (b) the equity investors do not have the characteristics of a controlling financial interest in the entity. Interpretation No. 46 applies immediately to all variable interest entities created after January 31, 2003. For variable interest entities created by public companies before February 1, 2003, Interpretation No. 46 must be applied no later than the beginning of the first interim or annual reporting period beginning after June 15, 2003. The initial determination of whether an entity is a variable interest entity shall be made as of the date at which a primary beneficiary becomes involved with the entity and reconsidered as of the date one of three triggering events described by Interpretation No. 46 occur. The Company does not believe that the adoption of this Interpretation will have a material effect on its financial statements.

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CONSOLIDATED BALANCE SHEETS

Vornado Realty Trust

(Amounts in thousands, except share and per share amounts)	December 31,	
	2002	2001
Assets:		
Real estate, at cost:		
Land	\$ 1,491,808	\$ 895,831
Buildings and improvements	5,948,255	3,480,249
Development costs and construction in progress	51,965	258,357
Leasehold improvements and equipment	67,666	55,774
Total	7,559,694	4,690,211
Less accumulated depreciation and amortization	(737,426)	(506,225)
Real estate, net	6,822,268	4,183,986
Cash and cash equivalents, including U.S. government obligations under repurchase agreements of \$33,393 and \$15,235	208,200	265,584
Escrow deposits and restricted cash	263,125	204,463
Marketable securities	42,525	126,774
Investments and advances to partially-owned entities, including Alexander's of \$193,879 and \$188,522	997,711	1,270,195
Due from officers	20,643	18,197
Accounts receivable, net of allowance for doubtful accounts of \$13,887 and \$8,831	65,754	47,406
Notes and mortgage loans receivable	86,581	258,555
Receivable arising from the straight-lining of rents, net of allowance of \$4,071 in 2002	240,449	202,754
Other assets	270,923	199,429
	\$ 9,018,179	\$ 6,777,343
Liabilities and Shareholders' Equity:		
Notes and mortgages payable	\$ 3,537,720	\$ 2,477,173
Senior Unsecured Notes due 2007, at fair value (\$34,245 in excess of accreted note balance in 2002)	533,600	—
Revolving credit facility	—	—
Accounts payable and accrued expenses	202,756	179,597
Officers compensation payable	16,997	6,708
Deferred credit	59,362	11,940
Other liabilities	3,030	51,895
Total liabilities	4,353,465	2,727,313
Minority interest of unitholders in the Operating Partnership	2,037,358	1,479,658
Commitments and contingencies		
Shareholders' equity:		
Preferred shares of beneficial interest:		
no par value per share; authorized 70,000,000 shares;		
Series A: liquidation preference \$50.00 per share; issued and outstanding 1,450,623 and 5,520,435 shares	72,535	276,024
Series B: liquidation preference \$25.00 per share; issued and outstanding 3,400,000 shares	81,805	81,805
Series C: liquidation preference \$25.00 per share; issued and outstanding 4,600,000 shares	111,148	111,148
Common shares of beneficial interest: \$.04 par value per share; authorized, 200,000,000 shares; issued and outstanding 108,629,736 and 99,035,023 shares	4,320	3,961
Additional capital	2,481,414	2,162,512
Distributions in excess of net income	(169,629)	(95,647)
	2,581,593	2,539,803
Deferred compensation shares earned but not yet delivered	66,660	38,253
Deferred compensation shares issued but not yet earned	(2,629)	—
Accumulated other comprehensive loss	(13,564)	(2,980)
Due from officers for purchase of common shares of beneficial interest	(4,704)	(4,704)
Total shareholders' equity	2,627,356	2,570,372
	\$ 9,018,179	\$ 6,777,343

See notes to consolidated financial statements.

CONSOLIDATED STATEMENTS OF INCOME

Vornado Realty Trust

Year Ended December 31,

(Amounts in thousands, except per share amounts)	2002	2001	2000
Revenues:			
Rentals	\$1,248,903	\$ 841,999	\$ 695,078
Expense reimbursements	159,978	133,114	120,056
Other income (including fee income from related parties of \$1,450, \$1,655, and \$1,418)	26,189	10,660	10,838
Total revenues	1,435,070	985,773	825,972
Expenses:			
Operating	541,596	398,969	318,360
Depreciation and amortization	205,826	123,862	99,846
General and administrative	98,458	72,572	47,911
Amortization of officer's deferred compensation expense	27,500	—	—
Costs of acquisitions and development not consummated	6,874	5,223	—
Total expenses	880,254	600,626	466,117
Operating income	554,816	385,147	359,855
Income applicable to Alexander's	29,653	25,718	17,363
Income from partially-owned entities	44,458	80,612	86,654
Interest and other investment income	31,685	54,385	32,926
Interest and debt expense (including amortization of deferred financing costs of \$8,339, \$8,458, and \$7,298)	(239,525)	(173,076)	(171,398)
Net loss on disposition of wholly-owned and partially-owned assets other than real estate	(17,471)	(8,070)	—
Minority interest:			
Perpetual preferred unit distributions	(72,500)	(70,705)	(62,089)
Minority limited partnership earnings	(64,899)	(39,138)	(38,320)
Partially-owned entities	(3,185)	(2,520)	(1,965)
Income before gains on sale of real estate and cumulative effect of change in accounting principle	263,032	252,353	223,026
Gains on sale of real estate	—	15,495	10,965
Cumulative effect of change in accounting principle	(30,129)	(4,110)	—
Net income	232,903	263,738	233,991
Preferred share dividends (including accretion of issuance expenses of \$958 in 2001 and \$2,875 in 2000)	(23,167)	(36,505)	(38,690)
Net Income: applicable to common shares	\$ 209,736	\$ 227,233	\$ 195,301
Income per common share—basic:			
Income before gains on sale of real estate and cumulative effect of change in accounting principle	\$ 2.26	\$ 2.42	\$ 2.14
Gains on sale of real estate	—	.17	.12
Cumulative effect of change in accounting principle	(.28)	(.04)	—
Net income per common share	\$ 1.98	\$ 2.55	\$ 2.26
Income per common share—diluted:			
Income before gains on sale of real estate and cumulative effect of change in accounting principle	\$ 2.18	\$ 2.34	\$ 2.08
Gains on sale of real estate	—	.17	.12
Cumulative effect of change in accounting principle	(.27)	(.04)	—
Net income per common share	\$ 1.91	\$ 2.47	\$ 2.20

See notes to consolidated financial statements.

CONSOLIDATED STATEMENTS OF SHAREHOLDERS' EQUITY

Vornado Realty Trust

(Amounts in thousands, except per share amounts)	Preferred Shares	Common Shares	Additional Capital	Distributions in Excess of Net Income	Accumulated Other Comprehensive Loss	Other	Shareholders' Equity	Comprehensive Income
Balance January 1, 2000	\$ 478,585	\$3,453	\$1,696,557	\$ (116,979)	\$ (1,448)	\$ (4,800)	\$ 2,053,368	
Net Income	—	—	—	233,991	—	—	233,991	\$233,991
Dividends paid on Preferred Shares								
Series A Preferred Shares (\$3.25 per share)	—	—	—	(21,689)	—	—	(21,689)	—
Series B Preferred Shares (\$2.125 per share)	—	—	—	(7,225)	—	—	(7,225)	—
Series C Preferred Shares (\$2.125 per share)	—	—	—	(9,776)	—	—	(9,776)	—
Dividends paid on common shares (\$1.97 per share)	—	—	—	(168,688)	—	—	(168,688)	—
Common shares issued under employees' share plan	—	15	9,913	—	—	—	9,928	—
Redemption of units for common shares	—	3	1,789	—	—	—	1,792	—
Accretion of issuance expenses on preferred shares	2,875	—	—	—	—	—	2,875	—
Common shares issued in connection with dividend reinvestment plan	—	1	1,025	—	—	—	1,026	—
Change in unrealized net loss on securities available for sale	—	—	—	—	(18,399)	—	(18,399)	(18,399)
Appreciation of securities held in officer's deferred compensation trust	—	—	—	—	(579)	—	(579)	(579)
Forgiveness of amount due from officers	—	—	—	—	—	96	96	—
Balance, December 31, 2000	481,460	3,472	1,709,284	(90,366)	(20,426)	(4,704)	2,078,720	\$215,013
Net Income	—	—	—	263,738	—	—	263,738	\$263,738
Dividends paid on Preferred Shares								
Series A Preferred Shares (\$3.25 per share)	—	—	—	(19,505)	—	—	(19,505)	—
Series B Preferred Shares (\$2.125 per share)	—	—	—	(7,225)	—	—	(7,225)	—
Series C Preferred Shares (\$2.125 per share)	—	—	—	(9,775)	—	—	(9,775)	—
Dividends paid on common shares (\$2.32 per share)	—	—	—	(201,813)	—	—	(201,813)	—
Dividends payable on common shares (\$.31 per share)	—	—	—	(30,701)	—	—	(30,701)	—
Common shares issued, net of shelf registration costs of \$260	—	391	376,542	—	—	—	376,933	—
Common shares issued under employees' share plan	—	12	9,947	—	—	—	9,959	—
Conversion of Series A Preferred Shares to common shares	(13,441)	15	13,426	—	—	—	—	—
Redemption of units for common shares	—	70	52,017	—	—	—	52,087	—
Accretion of issuance expenses on preferred shares	958	—	—	—	—	—	958	—
Common shares issued in connection with dividend reinvestment plan	—	1	1,296	—	—	—	1,297	—
Change in unrealized net loss on securities available for sale	—	—	—	—	18,178	—	18,178	18,178
Deferred compensation shares earned but not yet delivered	—	—	—	—	—	38,253	38,253	—
Pension obligations	—	—	—	—	(732)	—	(732)	(732)
Balance, December 31, 2001	\$ 468,977	\$3,961	\$2,162,512	\$ (95,647)	\$ (2,980)	\$33,549	\$2,570,372	\$281,184

See notes to consolidated financial statements.

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CONSOLIDATED STATEMENTS OF SHAREHOLDERS' EQUITY *continued*

Vornado Realty Trust

(Amounts in thousands, except per share amounts)	Preferred Shares	Common Shares	Additional Capital	Distributions in Excess of Net Income	Accumulated Other Comprehensive Loss	Other	Shareholders' Equity	Comprehensive Income
Balance, December 31, 2001	\$ 468,977	\$3,961	\$2,162,512	\$ (95,647)	\$ (2,980)	\$33,549	\$2,570,372	\$281,184
Net Income	—	—	—	232,903	—	—	232,903	\$232,903
Dividends paid on Preferred Shares								
Series A Preferred Shares (\$3.25 per share)	—	—	—	(6,167)	—	—	(6,167)	—
Series B Preferred Shares (\$2.125 per share)	—	—	—	(7,225)	—	—	(7,225)	—
Series C Preferred Shares (\$2.125 per share)	—	—	—	(9,775)	—	—	(9,775)	—
Net proceeds from issuance of common shares	—	56	56,397	—	—	—	56,453	—
Conversion of Series A Preferred shares to common shares	(203,489)	225	203,264	—	—	—	—	—
Deferred compensation shares	—	2	2,627	—	—	25,778	28,407	—
Dividends paid on common shares (\$2.97 per share, including \$.31 for 2001)	—	—	—	(314,419)	—	—	(314,419)	—
Reversal of dividends payable on common shares in 2001 (\$.31 per share)	—	—	—	30,701	—	—	30,701	—
Common shares issued under employees' share plan	—	36	24,349	—	—	—	24,385	—
Redemption of units for common shares	—	38	30,380	—	—	—	30,418	—
Common shares issued in connection with dividend reinvestment plan	—	2	1,885	—	—	—	1,887	—
Change in unrealized net loss on securities available for sale	—	—	—	—	(8,936)	—	(8,936)	(8,936)
Other non-cash changes, primarily pension obligations	—	—	—	—	(1,648)	—	(1,648)	(1,648)
Balance, December 31, 2002	\$ 265,488	\$4,320	\$2,481,414	\$ (169,629)	\$ (13,564)	\$59,327	\$2,627,356	\$222,319

See notes to consolidated financial statements.

CONSOLIDATED STATEMENTS OF CASH FLOWS

Vornado Realty Trust

(Amounts in thousands)	Year Ended December 31,		
	2002	2001	2000
Cash Flows from Operating Activities:			
Net income	\$ 232,903	\$ 263,738	\$ 233,991
Adjustments to reconcile net income to net cash provided by operating activities:			
Cumulative effect of change in accounting principle	30,129	4,110	—
Minority interest	140,584	112,363	102,374
Amortization of officer's deferred compensation	27,500	—	—
Net loss on dispositions of wholly-owned and partially-owned assets other than real estate	17,471	8,070	—
Costs of acquisitions and development not consummated	6,874	5,223	—
Gains on sale of real estate	—	(15,495)	(10,965)
Depreciation and amortization (including debt issuance costs)	205,826	123,862	99,846
Straight-lining of rental income	(36,478)	(27,230)	(32,206)
Amortization of below market leases, net	(12,634)	—	—
Equity in income of Alexander's	(29,653)	(25,718)	(17,363)
Equity in income of partially-owned entities	(44,458)	(80,612)	(86,654)
Changes in operating assets and liabilities	(38,239)	19,374	(39,102)
Net cash provided by operating activities	499,825	387,685	249,921
Cash Flows from Investing Activities:			
Development costs and construction in progress	(63,619)	(145,817)	(35,701)
Acquisitions of real estate and other	(23,665)	(11,574)	(199,860)
Additions to real estate	(96,018)	(67,090)	(136,081)
Investments in partially-owned entities	(100,882)	(109,332)	(99,974)
Proceeds from sale of real estate	—	162,045	47,945
Investments in notes and mortgage loans receivable	(56,935)	(83,879)	(144,225)
Repayment of notes and mortgage loans receivable	124,500	64,206	5,222
Cash restricted, primarily mortgage escrows	(21,471)	9,896	(183,788)
Distributions from partially-owned entities	126,077	114,218	68,799
Real estate deposits	—	—	4,819
Purchases of marketable securities	—	(14,325)	(26,531)
Proceeds from sale or maturity of securities available for sale	87,896	1,930	—
Net cash used in investing activities	(24,117)	(79,722)	(699,375)
Cash Flows from Financing Activities:			
Proceeds from borrowings	628,335	554,115	1,195,108
Repayments of borrowings	(731,238)	(835,257)	(633,655)
Costs of refinancing debt	(3,970)	(3,394)	(18,445)
Redemption of perpetual preferred units	(25,000)	—	—
Proceeds from issuance of preferred units	—	52,673	204,750
Proceeds from issuance of common shares	56,453	377,193	—
Dividends paid on common shares	(314,419)	(201,813)	(168,688)
Dividends paid on preferred shares	(23,167)	(35,547)	(35,815)
Distributions to minority partners	(146,358)	(98,594)	(80,397)
Exercise of share options	26,272	11,256	10,955
Net cash (used in) provided by financing activities	(533,092)	(179,368)	473,813
Net increase (decrease) in cash and cash equivalents	(57,384)	128,595	24,359
Cash and cash equivalents at beginning of year	265,584	136,989	112,630
Cash and cash equivalents at end of year	\$ 208,200	\$ 265,584	\$ 136,989
Supplemental Disclosure of Cash Flow Information:			
Cash payments for interest (including capitalized interest of \$6,677, \$12,171 and \$12,269)	\$ 247,048	\$ 171,166	\$ 165,325
Non-Cash Transactions:			
Financing assumed in acquisitions	\$ 1,596,903	\$ —	\$ 46,640
Class A units issued in connection with acquisitions	625,234	18,798	9,192
Unrealized (loss) gain on securities available for sale	860	9,495	(18,399)
(Appreciation) depreciation of securities held in officer's deferred compensation trust	—	(3,023)	(579)

See notes to consolidated financial statements.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Vornado Realty Trust

1. ORGANIZATION AND BUSINESS

Vornado Realty Trust is a fully-integrated real estate investment trust (“REIT”). Vornado conducts its business through Vornado Realty L.P., (“the Operating Partnership”). Vornado is the sole general partner of, and owned approximately 79% of the common limited partnership interest in, the Operating Partnership at February 3, 2003. All references to the “Company” and “Vornado” refer to Vornado Realty Trust and its consolidated subsidiaries, including the Operating Partnership.

The Company currently owns directly or indirectly:

Office Properties (“Office”):

- (i) all or portions of 74 office properties aggregating approximately 27.7 million square feet in the New York City metropolitan area (primarily Manhattan) and in the Washington, DC and Northern Virginia area;

Retail Properties (“Retail”):

- (ii) 62 retail properties in six states and Puerto Rico aggregating approximately 12.5 million square feet, including 1.8 million square feet built by tenants on land leased from the Company;

Merchandise Mart Properties:

- (iii) 8.6 million square feet of showroom and office space, including the 3.4 million square foot Merchandise Mart in Chicago;

Temperature Controlled Logistics:

- (iv) a 60% interest in the Vornado Crescent Portland Partnership that owns 88 cold storage warehouses nationwide with an aggregate of approximately 441.5 million cubic feet of refrigerated space leased to AmeriCold Logistics;

Other Real Estate Investments:

- (v) 33.1% of the outstanding common stock of Alexander’s, Inc. (“Alexander’s”);
- (vi) the Hotel Pennsylvania in New York City, consisting of a hotel portion containing 1.0 million square feet with 1,700 rooms and a commercial portion containing .4 million square feet of retail and office space;
- (vii) a 21.7% interest in The Newkirk Master Limited Partnership, which owns office, retail and industrial properties net leased primarily to credit-rated tenants, and various debt interests in such properties;
- (viii) eight dry warehouse/industrial properties in New Jersey containing approximately 2.0 million square feet; and
- (ix) other investments, including interests in other real estate, marketable securities and loans and notes receivable.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Basis of Presentation: The accompanying consolidated financial statements include the accounts of Vornado Realty Trust and its majority-owned subsidiary, Vornado Realty L.P., as well as entities in which the Company has a 50% or greater interest, provided that the Company exercises direct or indirect control. All significant intercompany amounts have been eliminated. The Company considers the guidance in APB 18, SOP 78-9 and EITF 96-16 in determining whether it does or does not control joint ventures on a case-by-case basis, taking into account board representation, management representation and authority and the contractual and substantive participating rights of its partners/members. If the approval of all of the partners/members is contractually required with respect to major decisions, such as operating and capital budgets, the sale, exchange or other disposition of any real property assets, the hiring of a Chief Executive Officer, the commencement, compromise or settlement of any lawsuit, legal proceeding or arbitration or the placement of any new or additional financing secured by any assets of the joint venture, then the Company does not control the venture and therefore will not consolidate the entity, despite the fact that it may own 50% or more of the relevant entity. This is the case with respect to Temperature Controlled Logistics, Monmouth Mall, 400 North LaSalle, MartParc Orleans, MartParc Wells, 825 Seventh Avenue and Starwood Ceruzzi. If the Company is able to unilaterally make major decisions for the partially owned entity and owns an interest greater than 50%, the Company has control and therefore consolidates the entity. The Company accounts for investments under the equity method when the Company's ownership interest is more than 20% but less than 50% and the Company does not exercise direct or indirect control. When partially-owned investments are in partnership form, the 20% threshold may be reduced. For all other investments, the Company uses the cost method. Equity investments are recorded initially at cost and subsequently adjusted for the Company's share of the net income or loss and cash contributions and distributions to or from these entities.

Prior to January 1, 2001, the Company's equity interests in partially-owned entities also included investments in preferred stock affiliates (corporations in which the Company owned all of the preferred stock and none of the common equity). Ownership of the preferred stock entitled the Company to substantially all of the economic benefits in the preferred stock affiliates. On January 1, 2001, the Company acquired the common stock of the preferred stock affiliates, which was owned by the Officers and Trustees of the Company, and converted them to taxable REIT subsidiaries. Accordingly, the Hotel portion of the Hotel Pennsylvania and the management companies (which provide services to the Company's business segments and operate the Trade Show business of the Merchandise Mart division) have been consolidated beginning January 1, 2001.

Management has made estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting periods. Actual results could differ from those estimates.

Reclassifications: Certain prior year balances have been reclassified in order to conform to current year presentation.

Real Estate: Real estate is carried at cost, net of accumulated depreciation and amortization. Betterments, major renewals and certain costs directly related to the acquisition, improvement and leasing of real estate are capitalized. Maintenance and repairs are charged to operations as incurred. For redevelopment of existing operating properties, the net book value of the existing property under redevelopment plus the cost for the construction and improvements incurred in connection with the redevelopment are capitalized to the extent the capitalized costs of the property do not exceed the estimated fair value of the redeveloped property when complete. If the cost of the redeveloped property, including the undepreciat-

Vornado Realty Trust

ed net book value of the property carried forward, exceeds the estimated fair value of redeveloped property, the excess is charged to expense. Depreciation is provided on a straight-line basis over the assets' estimated useful lives which range from 7 to 40 years. Tenant allowances are amortized on a straight-line basis over the lives of the related leases, which approximates the useful lives of the assets. Additions to real estate include interest expense capitalized during construction of \$6,677,000, \$12,171,000, and \$12,269,000 for the years ended December 31, 2002, 2001, and 2000.

Upon acquisitions of real estate, the Company assesses the fair value of acquired assets (including land, buildings, tenant improvements, acquired above and below market leases and the origination cost of acquired in-place leases in accordance with SFAS No. 141) and acquired liabilities, and allocate purchase price based on these assessments. The Company assesses fair value based on estimated cash flow projections that utilize appropriate discount and capitalization rates and available market information. Estimates of future cash flows are based on a number of factors including the historical operating results, known trends, and market/economic conditions that may affect the property. The Company's properties are reviewed for impairment if events or circumstances change indicating that the carrying amount of the assets may not be recoverable. If the Company incorrectly estimates the values at acquisition or the undiscounted cash flows, initial allocations of purchase price and future impairment charges may be different.

Cash and Cash Equivalents: Cash and cash equivalents consist of highly liquid investments purchased with original maturities of three months or less. Cash and cash equivalents does not include cash escrowed under loan agreements and cash restricted in connection with an officer's deferred compensation payable.

Allowance for doubtful accounts: The Company periodically evaluates the collectibility of amounts due from tenants and maintains an allowance for doubtful accounts for estimated losses resulting from the inability of tenants to make required payments under the lease agreements. The Company also maintains an allowance for receivables arising from the straight-lining of rents. This receivable arises from earnings recognized in excess of amounts currently due under the lease agreements. Management exercises judgment in establishing these allowances and considers payment history and current credit status in developing these estimates.

Marketable Securities: The Company has classified debt and equity securities which it intends to hold for an indefinite period of time (including warrants to acquire equity securities) as securities available for sale; equity securities it intends to buy and sell on a short term basis as trading securities; and preferred stock investments as securities held to maturity. Unrealized gains and losses on trading securities are included in earnings. Unrealized gains and losses on securities available for sale are included as a component of shareholders' equity and other comprehensive income. Realized gains or losses on the sale of securities are recorded based on specific identification. A portion of the Company's preferred stock investments are redeemable and accounted for in accordance with EITF 99-20 "Recognition of Interest Income and Impairment on Purchased and Retained Beneficial Interests in Securitized Financial Assets." Income is recognized by applying the prospective method of adjusting the yield to maturity based on an estimate of future cash flows. If the value of the investment based on the present value of the future cash flows is less than the Company's carrying amount, the investments will be written-down to fair value through earnings. Investments in securities of non-publicly traded companies are reported at cost, as they are not considered marketable under SFAS No. 115.

At December 31, 2002 and 2001, marketable securities had an aggregate cost of \$41,665,000 and \$117,284,000 and an aggregate market value of \$42,525,000 and \$126,774,000 (of which \$0 and

\$13,888,000 represents trading securities; \$2,020,000 and \$49,763,000 represents securities available for sale; and \$40,505,000 and \$63,123,000 represent securities held to maturity). Gross unrealized gains and losses were \$860,000 and \$0 at December 31, 2002, and \$14,738,000 and \$5,243,000 at December 31, 2001.

Notes and Mortgage Loans Receivable: The Company's policy is to record mortgages and notes receivable at the stated principal amount less any discount or premiums. The Company accretes or amortizes any discounts or premiums over the life of the related loan receivable utilizing the effective interest method. The Company evaluates the collectibility of both interest and principal of each of its loans, if circumstances warrant, to determine whether it is impaired. A loan is considered to be impaired, when based on current information and events, it is probable that the Company will be unable to collect all amounts due according to the existing contractual terms. When a loan is considered to be impaired, the amount of the loss accrual is calculated by comparing the recorded investment to the value determined by discounting the expected future cash flows at the loan's effective interest rate or, as a practical expedient, to the value of the collateral if the loan is collateral dependent. Interest on impaired loans is recognized on a cash basis.

Deferred Charges: Direct financing costs are deferred and amortized over the terms of the related agreements as a component of interest expense. Direct costs related to leasing activities are capitalized and amortized on a straight-line basis over the lives of the related leases. All other deferred charges are amortized on a straight-line basis, which approximates the effective interest rate method, in accordance with the terms of the agreements to which they relate.

Fair Value of Financial Instruments: All financial instruments of the Company are reflected in the accompanying consolidated balance sheets at amounts which, in management's estimation, based upon an interpretation of available market information and valuation methodologies (including discounted cash flow analyses with regard to fixed rate debt) are considered appropriate. The fair value of the Company's debt is approximately \$178,566,000 in excess of the aggregate carrying amount at December 31, 2002. Such fair value estimates are not necessarily indicative of the amounts that would be realized upon disposition of the Company's financial instruments.

Derivative Instruments And Hedging Activities: Statement of Financial Accounting Standards No. 133, *Accounting for Derivative Instruments and Hedging Activities* (SFAS 133), as amended and interpreted, establishes accounting and reporting standards for derivative instruments, including certain derivative instruments embedded in other contracts, and for hedging activities. As required by SFAS 133, the Company records all derivatives on the balance sheet at fair value. The accounting for changes in the fair value of derivatives depends on the intended use of the derivative and the resulting designation. Derivatives used to hedge the exposure to changes in the fair value of an asset, liability, or firm commitment attributable to a particular risk, such as interest rate risk, are considered fair value hedges. Derivatives used to hedge the exposure to variability in expected future cash flows, or other types of forecasted transactions, are considered cash flow hedges. The cumulative effect of implementing SFAS No. 133 on January 1, 2001, was \$4,110,000.

For derivatives designated as fair value hedges, changes in the fair value of the derivative and the hedged item related to the hedged risk are recognized in earnings. For derivatives designated as cash flow hedges, the effective portion of changes in the fair value of the derivative is initially reported in other comprehensive income (outside of earnings) and subsequently reclassified to earnings when the hedged transaction affects earnings, and the ineffective portion of changes in the fair value of the derivative is recognized directly in earnings. The Company assesses the effectiveness of each hedging relationship by comparing the changes in fair value or cash flows of the derivative hedging instrument with the changes in fair value or

Vornado Realty Trust

cash flows of the designated hedged item or transaction. For derivatives not designated as hedges, changes in fair value are recognized in earnings. Additionally, the Company does not use derivatives for trading or speculative purposes and currently does not have any derivatives that are not designated as hedges.

On June 27, 2002, the Company entered into interest rate swaps that effectively converted the interest rate on the \$500,000,000 senior unsecured notes due 2007 from a fixed rate of 5.625% to a floating rate of LIBOR plus .7725%, based upon the trailing 3 month LIBOR rate (2.18% at December 31, 2002). These swaps were designated and effective as fair value hedges, with a fair value of \$34,245,000 at December 31, 2002, which is included in Other Assets on the Company's balance sheet. Accounting for these swaps also requires the Company to recognize changes in the fair value of the debt during each reporting period. At December 31, 2002, the fair value adjustment of \$34,245,000, based on the fair value of the swaps, is included in the balance of the Senior Unsecured Notes. Because the hedging relationship qualifies for the "short-cut" method, the hedge ineffectiveness on these fair value hedges was recognized during 2002.

Revenue Recognition: The Company has the following revenue sources and revenue recognition policies:

Base Rents—income arising from tenant leases. These rents are recognized over the non-cancelable term of the related leases on a straight-line basis which includes the effects of rent steps and free rent abatements under the leases.

Percentage Rents—income arising from retail tenant leases which are contingent upon the sales of the tenant exceeding a defined threshold. These rents are recognized in accordance with SAB 101, which states that this income is to be recognized only after the contingency has been removed (i.e., sales thresholds have been achieved).

Hotel Revenues—income arising from the operation of the Hotel Pennsylvania which consists of rooms revenue, food and beverage revenue, and banquet revenue. Income is recognized when rooms are occupied. Food and beverage and banquet revenue are recognized when the services have been rendered.

Trade Show Revenues—income arising from the operation of trade shows, including rentals of booths. This revenue is recognized in accordance with the booth rental contracts when the trade shows have occurred.

Expense Reimbursement Income—income arising from tenant leases which provide for the recovery of all or a portion of the operating expenses and real estate taxes of the respective property. This income is accrued in the same periods as the expenses are incurred. Contingent rents are not recognized until realized.

Income Taxes: The Company operates in a manner intended to enable it to continue to qualify as a REIT under Sections 856-860 of the Internal Revenue Code of 1986, as amended. Under those sections, a REIT which distributes at least 90% of its REIT taxable income as a dividend to its shareholders each year and which meets certain other conditions will not be taxed on that portion of its taxable income which is distributed to its shareholders. The Company will distribute to its shareholders 100% of its taxable income and therefore, no provision for Federal income taxes is required. Dividend distributions for the years ended December 31, 2002, 2001 and 2000, were characterized for Federal income tax purposes as ordinary income.

The Company owns stock in corporations that have elected to be treated for Federal income tax purposes, as taxable REIT subsidiaries ("TRS"). The value of the combined TRS stock cannot and does not exceed 20% of the value of the Company's total assets. A TRS is taxable on its net income at regular corporate tax rates. For the 2002 tax year, the total income tax is approximately \$1,430,000.

The following table reconciles net income to estimated taxable income for the year ended December 31, 2002.

Net income applicable to common shares	\$232,903,000
Depreciation and amortization	69,360,000
Straight-line rent adjustments	(30,687,000)
Book to tax differences in earnings of partially-owned entities	(21,958,000)
Amortization of officer's deferred compensation	22,916,000
Primestone impairment loss	15,071,000
Stock option expense	(12,400,000)
Amortization of acquired below market leases, net of above market leases	(10,528,000)
Other	5,219,000
Estimated taxable income	\$269,896,000

The net basis of the Company's assets and liabilities for tax purposes is approximately \$2,822,000,000 lower than the amount reported for financial statement purposes.

At December 31, 2002, the Company had a capital loss carryover of approximately \$73,000,000. The capital loss carryover is available to offset future capital gains that would otherwise be required to be distributed as dividends to shareholders.

Amounts Per Share: Basic earnings per share is computed based on weighted average shares outstanding. Diluted earnings per share considers the effect of outstanding options, warrants and convertible or redeemable securities.

Stock-Based Compensation: In 2002 and prior years, the Company accounted for stock-based compensation using the intrinsic value method. Under the intrinsic value method compensation cost is measured as the excess, if any, of the quoted market price of the Company's stock at the date of grant over the exercise price of the option granted. Compensation cost for stock options, if any, is recognized ratably over the vesting period. The Company's policy is to grant options with an exercise price equal to the quoted market price of the Company's stock on the grant date. Accordingly, no compensation cost has been recognized for the Company's stock option plans. See Note 8—Employees' Share Option Plan for details of the Company's outstanding employee share options and the related pro forma stock-based employee compensation cost. Effective January 1, 2003, the Company adopted SFAS No. 123 "Accounting for Stock Based Compensation" as amended by SFAS No. 148 "Accounting for Stock-Based Compensation—Transition and Disclosure." The Company will adopt SFAS No. 123 prospectively by valuing and accounting for employee stock options granted in 2003 and thereafter. The Company will utilize a binomial valuation model and appropriate market assumptions to determine the value of each grant. Stock-based compensation expense will be recognized on a straight-line basis over the vesting period of the respective grants.

In addition to employee stock option grants, the Company has also granted restricted shares to certain of its employees that vest over a three to five year period. The Company records the value of each restricted share award as stock-based compensation expense based on the Company's closing stock price on the NYSE on the date of grant on a straight-line basis over the vesting period. As of December 31, 2002, the Company has 250,927 restricted shares or rights to receive restricted shares outstanding to employees of the Company, excluding 626,566 shares issued to the Company's President in connection with his employment agreement. The Company recognized \$1,868,000 of stock-based compensation expense in 2002 for the portion of these shares that vested during the year.

Vornado Realty Trust

Recently Issued Accounting Standards

SFAS No. 141—*Business Combinations* requires companies to account for the value of leases acquired and the costs of acquiring such leases separately from the value of the real estate for all acquisitions subsequent to July 1, 2001. Accordingly, the Company has evaluated the leases in place for (i) the remaining 66% of CESCRO it did not previously own which it acquired on January 1, 2002, (ii) the remaining 50% of the Las Catalinas Mall it did not previously own which it acquired on September 23, 2002 and (iii) a 50% interest in the Monmouth Mall which it acquired on October 10, 2002, to determine whether they were acquired at market, above market or below market. The Company's evaluations were based on (i) the differences between contractual rentals and the estimated market rents over the applicable lease term discounted back to the date of acquisition utilizing a discount rate adjusted for the credit risk associated with the respective tenants and (ii) the estimated cost of acquiring such leases giving effect to the Company's history of providing tenant improvements and paying leasing commissions.

As a result of its evaluations, as of December 31, 2002, the Company has recorded a deferred credit of \$48,430,000 representing the value of acquired below market leases, deferred charges of \$15,976,000 for the value of acquired above market leases and \$3,621,000 for origination costs. In addition, in the year ended December 31, 2002 the Company has recognized property rentals of \$12,634,000, for the amortization of below market leases net of above market leases, and depreciation expense of \$1,214,000 for the amortization of the lease origination costs and additional building depreciation resulting from the reallocation of the purchase price of the applicable properties.

SFAS No. 142—Goodwill and Other Intangible Assets

In June 2001, the Financial Accounting Standards Board ("FASB") issued Statement of Financial Accounting Standard ("SFAS") No. 142, *Goodwill and Other Intangible Assets* (effective January 1, 2002). SFAS No. 142 specifies that goodwill and some intangible assets will no longer be amortized but instead be subject to periodic impairment testing. SFAS No. 142 provides specific guidance for impairment testing of these assets and removes them from the scope of SFAS No. 121, *Accounting for the Impairment of Long-Lived Assets*. The Company's goodwill balance on December 31, 2001 of \$30,129,000 consisted of \$14,639,000 related to the Hotel Pennsylvania acquisition and \$15,490,000 related to the acquisition of the Temperature Controlled Logistics businesses.

Prior to January 1, 2002, the Company performed impairment testing in accordance with SFAS 121. The Company reviewed for impairment whenever events or changes in circumstances indicated that the carrying amount of an asset may not be recoverable. Given the decrease in the estimated market values and the deteriorating performance of Hotel Pennsylvania and Temperature Controlled Logistics, the Company performed a review for recoverability estimating the future cash flows expected to result from the use of the assets and their eventual disposition. As of December 31, 2001, the sum of the expected cash flows (undiscounted and without interest charges) exceeded the carrying amounts of goodwill, and therefore no impairments were recognized.

Upon adoption of SFAS 142 on January 1, 2002, the Company tested the goodwill for impairment at the reporting level unit utilizing the prescribed two-step method. The first step compared the fair value of the reporting unit (determined based on a discounted cash flow approach) with its carrying amount. As the carrying amount of the reporting unit exceeded its fair value, the second step of the impairment test was performed to measure the impairment loss. The second step compared the implied fair value of goodwill with the carrying amount of the goodwill. As the carrying amounts of the goodwill exceed the fair values, on January 1, 2002 the Company wrote-off all of the goodwill of the Hotel and the Temperature Controlled Logistics businesses as an impairment loss totaling \$30,129,000. The write-off has been reflect-

ed as a cumulative effect of change in accounting principle on the income statement. Earnings allocable to the minority interest have been reduced by their pro-rata share of the write-off of goodwill.

Previously reported “Income before gains on sale of real estate and cumulative effect of change in accounting principle” and “Net income applicable to common shares” for the year ended December 31, 2001 would have been approximately \$972,000 higher, or \$2.35 and \$2.48 per share, if such goodwill was not amortized in the prior year.

SFAS No. 143—Accounting for Asset Retirement Obligations and SFAS No. 144—Accounting for the Impairment or Disposal of Long-Lived Assets

In August 2001, the FASB issued SFAS No. 143, *Accounting for Asset Retirement Obligations* (effective January 1, 2003) and SFAS No. 144, *Accounting for the Impairment or Disposal of Long-Lived Assets* (effective January 1, 2002). SFAS No. 143 requires the recording of the fair value of a liability for an asset retirement obligation in the period which it is incurred. SFAS No. 144 supersedes current accounting literature and now provides for a single accounting model for long-lived assets to be disposed of by sale and requires discontinued operations presentation for disposals of a “component” of an entity. The adoption of these statements did not have a material effect on the Company’s financial statements; however, under SFAS No. 144, if the Company were to dispose of a material operating property, such property’s results of operations will have to be separately disclosed as discontinued operations in the Company’s financial statements.

SFAS No. 145—Rescission of SFAS No. 4, 44, and 64, Amendment of SFAS No. 13, and Technical Corrections

In April 2002, the FASB issued SFAS No. 145, *Rescission of SFAS No. 4, 44, and 64, Amendment of SFAS No. 13, and Technical Corrections*. SFAS No. 145 requires, among other things, (i) that the modification of a lease that results in a change of the classification of the lease from capital to operating under the provisions of SFAS No. 13 be accounted for as a sale-leaseback transaction and (ii) the reporting of gains or losses from the early extinguishment of debt as extraordinary items only if they met the criteria of Accounting Principles Board Opinion No. 30, *Reporting the Results of Operations*. The rescission of SFAS No. 4 is effective January 1, 2003. The amendment of SFAS No. 13 is effective for transactions occurring on or after May 15, 2002. The adoption of this statement did not have a material effect on the Company’s financial statements.

SFAS No. 146—Accounting for Costs Associated with Exit or Disposal Activities

In July 2002, the FASB issued SFAS No. 146, *Accounting for Costs Associated with Exit or Disposal Activities* (effective January 1, 2003). SFAS No. 146 replaces current accounting literature and requires the recognition of costs associated with exit or disposal activities when they are incurred rather than at the date of a commitment to an exit or disposal plan. The Company does not anticipate that the adoption of this statement will have a material effect on the Company’s financial statements.

SFAS No. 148—Accounting for Stock-Based Compensation—Transition and Disclosure—An Amendment of FASB Statement No. 123

On August 7, 2002, the Company announced that beginning January 1, 2003, it will expense the cost of employee stock options in accordance with SFAS No. 123, *Accounting For Stock-Based Compensation*. In December 2002, the FASB issued Statement No. 148—*Accounting for Stock-Based Compensation—Transition and Disclosure—An Amendment of FASB Statement No. 123* to amend the transition and disclosure provisions of SFAS No. 123. Specifically, SFAS No. 123, as amended, would permit two additional transition methods for entities that adopt the fair value method of accounting for stock based employee compensation. The Company will adopt SFAS No. 123 prospectively by valuing and accounting for employee stock options

Vornado Realty Trust

granted in 2003 and thereafter. The Company will utilize a binomial valuation model and appropriate market assumptions to determine the value of each grant. Stock-based compensation expense will be recognized on a straight-line basis over the vesting period of the respective grants.

FASB Interpretation No. 45—Guarantor’s Accounting and Disclosure Requirements for Guarantees, Including Indirect Guarantees of Indebtedness of Others

In November 2002, the FASB issued Interpretation No. 45—*Guarantor’s Accounting and Disclosure Requirements for Guarantees, Including Indirect Guarantees of Indebtedness of Others*, which elaborates on the disclosures to be made by a guarantor in its interim and annual financial statements about its obligations under certain guarantees that it has issued. The initial recognition and measurement provisions of this Interpretation are applicable on a prospective basis to guarantees issued or modified after December 31, 2002. The Company believes that the adoption of this interpretation will not have a material effect to the financial statements.

FASB Interpretation No. 46—Consolidation of Variable Interest Entities

In January 2003, the FASB issued Interpretation No. 46—*Consolidation of Variable Interest Entities*, which requires the consolidation of an entity by an enterprise (i) if that enterprise, known as a “primary beneficiary,” has a variable interest that will absorb a majority of the entity’s expected losses if they occur, receive a majority of the entity’s expected residual returns if they occur, or both and (ii) if the entity is a variable interest entity, as defined by Interpretation No. 46. An entity is a variable interest entity if (a) the total equity investment at risk in the entity is not sufficient to permit the entity to finance its activities without additional subordinated financial support from other parties or (b) the equity investors do not have the characteristics of a controlling financial interest in the entity. Interpretation No. 46 applies immediately to all variable interest entities created after January 31, 2003. For variable interest entities created by public companies before February 1, 2003, Interpretation No. 46 must be applied no later than the beginning of the first interim or annual reporting period beginning after June 15, 2003. The initial determination of whether an entity is a variable interest entity shall be made as of the date at which a primary beneficiary becomes involved with the entity and reconsidered as of the date one of three triggering events described by Interpretation No. 46 occur. The Company does not believe that the adoption of this Interpretation will have a material effect on its financial statements.

3. ACQUISITIONS AND DISPOSITIONS

The Company completed approximately \$1,834,600,000 of real estate acquisitions or investments in 2002 and \$19,200,000 in 2001. These acquisitions were consummated through subsidiaries or preferred stock affiliates of the Company. Acquisitions of business were recorded under the purchase method of accounting. Related net assets and results of operations have been included in these financial statements since their respective dates of acquisition. The pro forma effect of the individual acquisitions and in the aggregate other than Charles E. Smith Commercial Realty were not material to the Company’s historical results of operations.

Acquisitions of individual properties are recorded as acquisitions of real estate assets. Acquisitions of businesses are accounted for under the purchase method of accounting. The purchase price for property acquisitions and businesses acquired is allocated to acquired assets and assumed liabilities using their relative fair values as of the acquisition date based on valuations and other studies. Initial valuations are subject to change until such information is finalized no later than 12 months from the acquisition date.

Office:*Charles E. Smith Commercial Realty Investment ("CESCR")*

On January 1, 2002, the Company completed the combination of CESCR with Vornado. CESCR has a dominant market position in the Washington, DC and Northern Virginia area, owning approximately 12.4 million square feet in 53 office properties as well as a highly competent management team. In the Company's opinion, the assets were acquired at below replacement cost and with below market leases. As a result of the combination, the Company will be in position to capitalize on the favorable supply/demand characteristics of the Washington, DC office markets. Prior to the combination, Vornado owned a 34% interest in CESCR. The consideration for the remaining 66% of CESCR was approximately \$1,600,000,000, consisting of 15.6 million newly issued Vornado Operating Partnership units and approximately \$1 billion of debt (66% of CESCR's total debt). The purchase price paid by the Company was determined based on the weighted average closing price of the equity issued to CESCR unitholders for the period beginning two business days before and ending two business days after the date the acquisition was agreed to and announced on October 19, 2001. The Company also capitalized as part of the basis of the assets acquired approximately \$32,000,000 for third party acquisition related costs, including advisory, legal and other professional fees that were contemplated at the time of the acquisition. The following table summarizes the estimated fair value of assets acquired and liabilities assumed at January 1, 2002, the date of acquisition.

(Amounts in thousands)

Land, buildings and improvements	\$1,681,000
Intangible deferred charges	36,000
Working capital	41,000
Total assets acquired	1,758,000
Mortgages and notes payable	1,023,000
Intangible deferred credit	62,000
Other liabilities	34,000
Total liabilities assumed	1,119,000
Net assets acquired	\$ 639,000

The Company's estimate of the weighted average useful life of acquired intangibles is approximately three years. This acquisition was recorded as a business combination under the purchase method of accounting. The purchase price was allocated to acquired assets and assumed liabilities using their relative fair values as of January 1, 2002 based on valuations and other studies. The operations of CESCR are consolidated into the accounts of the Company beginning January 1, 2002. Prior to this date the Company accounted for its 34% interest on the equity method.

The unaudited pro forma information set forth below presents the condensed consolidated statements of income for the Company for the year ended December 31, 2001 as if the following transactions had occurred on January 1, 2001, (i) the acquisition of CESCR described above and (ii) the Company's November 21, 2001 sale of 9,775,000 common shares and the use of proceeds to repay indebtedness.

Vornado Realty Trust

Condensed Consolidated Statements of Income

(in thousands, except per-share amounts)	For the Year Ended December 31,	
	2002	Pro Forma 2001
Revenues	\$1,435,070	\$1,384,933
Income before gains on sale of real estate and cumulative effect of change in accounting principle	\$ 263,032	\$ 284,420
Gains on sale of real estate	—	15,495
Cumulative effect of change in accounting principle	(30,129)	(4,110)
Net income	232,903	295,805
Preferred share dividends	(23,167)	(36,505)
Net income applicable to common shares	\$ 209,736	\$ 259,300
Net income per common share—basic	\$ 1.98	\$ 2.62
Net income per common share—diluted	\$ 1.91	\$ 2.55

Crystal Gateway One

On July 1, 2002, the Company acquired a 360,000 square foot office building from a limited partnership, which is approximately 50% owned by Mr. Robert H. Smith and Mr. Robert P. Kogod and members of the Smith and Kogod families, trustees of the Company, in exchange for approximately 325,700 newly issued Vornado Operating Partnership units (valued at \$13,679,000) and the assumption of \$58,500,000 of debt. The building is located in the Crystal City complex in Arlington, Virginia where the Company already owns 24 office buildings containing over 6.9 million square feet, which it acquired on January 1, 2002, in connection with the Company's acquisition of CESCO. The operations of Crystal Gateway One are consolidated into the accounts of the Company from the date of acquisition.

Building Maintenance Service Company

On January 1, 2003, the Company acquired the Building Maintenance Service Company for \$13,000,000 in cash, which provides cleaning and related services and security services to office properties, including the Company's Manhattan office properties. This company was previously owned by the estate of Bernard Mendik and certain other individuals including Mr. Greenbaum, one of the Company's executive officers. This acquisition was recorded as a business combination under the purchase method of accounting.

Retail

Las Catalinas Mall

On September 23, 2002, the Company increased its interest in the Las Catalinas Mall located in Caguas, Puerto Rico (San Juan area) to 100% by acquiring the 50% of the mall and 25% of the Kmart anchor store it did not already own. The purchase price was \$48,000,000, of which \$16,000,000 was paid in cash and \$32,000,000 was debt assumed. The Las Catalinas Mall, which opened in 1997, contains 492,000 square feet, including a 123,000 square foot Kmart and a 138,000 square foot Sears owned by the tenant. Prior to September 23, 2002, the Company accounted for its investment on the equity method. Subsequent to this date the operations of Las Catalinas are consolidated into the accounts of the Company.

Monmouth Mall

On October 10, 2002, a joint venture in which the Company has a 50% interest, acquired the Monmouth Mall, an enclosed super regional shopping center located in Eatontown, New Jersey containing approximately 1.5 million square feet, including four department stores, three of which aggregating 731,000 square feet are owned by the tenants. The purchase price was approximately \$164,700,000, including transaction costs of \$4,400,000. The Company made a \$7,000,000 cash investment in the form of common equity to the venture and provided it with cash of \$23,500,000 representing preferred equity yielding 14%. The venture financed the purchase of the Mall with \$135,000,000 of floating rate debt at LIBOR plus 2.05%, with a LIBOR floor of 2.50% on \$35,000,000, a three year term and two one-year extension options. The Company accounts for its investment on the equity method.

Other:

On December 31, 2002, the Company and Crescent Real Estate Equities formed a joint venture to acquire the Carthage, Missouri and Kansas City, Kansas quarries from AmeriCold Logistics, the Company's tenant at the cold storage warehouses (Temperature Controlled Logistics) facilities for \$20,000,000 in cash (appraised value). The Company contributed cash of \$8,800,000 to the joint venture representing its 44% interest. The Company accounts for its investment in the venture on the equity method.

Dispositions:

The following table sets forth the details of sales, dispositions, write-offs and other similar transactions for the years ended December 31, 2002, 2001 and 2000:

(\$ in thousands)	2002	2001	2000
Wholly-owned and partially-owned assets other than depreciable real estate:			
Wholly-owned Assets:			
Gain on transfer of mortgages	\$ 2,096	\$ —	\$ —
Net gain on sale of air rights	1,688	—	—
Gain on sale of Kinzie Park Condominium units	2,156	—	—
Net gain on sale of marketable securities	12,346	—	—
Primestone foreclosure and impairment losses	(35,757)	—	—
Write-off of investments in technology companies	—	(16,513)	—
Partially-owned Assets:			
After-tax net gain on sale of Park Laurel condominium units	—	15,657	—
Write-off of net investment in the Russian Tea Room ("RTR")	—	(7,374)	—
Other	—	160	—
Net loss on disposition of wholly-owned and partially-owned assets other than real estate	\$ (17,471)	\$ (8,070)	\$ —
Net gains on sale of real estate			
Condemnation proceedings	\$ —	\$ 3,050	\$ —
Sale of 570 Lexington Avenue	—	12,445	—
Sale of other real estate	—	—	10,965
Net gain on sale of real estate	\$ —	\$ 15,495	\$ 10,965

Vornado Realty Trust

Gain on Transfer of Mortgages

In the year ended December 31, 2002, the Company recorded a net gain of approximately \$2.1 million resulting from payments to the Company by third parties that assumed certain of the Company's mortgages. Under these transactions the Company paid to the third parties that assumed the Company's obligations the outstanding amounts due under the mortgages and the third parties paid the Company for the benefit of assuming the mortgages. The Company has been released by the creditors underlying these loans.

Net Gain on Sale of Air Rights

The Company constructed a \$16.3 million community facility and low-income residential housing development (the "30th Street Venture"), in order to receive 163,728 square feet of transferable development rights, generally referred to as "air rights." The Company donated the building to a charitable organization. The Company sold 106,796 square feet of these air rights to third parties at an average price of \$120 per square foot. An additional 28,821 square feet of air rights was sold to Alexander's at a price of \$120 per square foot for use at Alexander's 59th Street development project (the "59th Street Project"). In each case, the Company received cash in exchange for air rights. The Company identified third party buyers for the remaining 28,111 square feet of air rights of the 30th Street Venture. These third party buyers wanted to use the air rights for the development of two projects located in the general area of 86th Street which was not within the required geographical radius of the construction site nor in the same Community Board as the low-income housing and community facility project. The 30th Street Venture asked Alexander's to sell 28,111 square feet of the air rights it already owned to the third party buyers (who could use them) and the 30th Street Venture would replace them with 28,111 square feet of air rights. In October 2002, the Company sold 28,111 square feet of air rights to Alexander's for an aggregate sales price of \$3,059,000 (an average of \$109 per square foot). Alexander's then sold an equal amount of air rights to the third party buyers for an aggregate sales price of \$3,339,000 (an average of \$119 per square foot).

Gain on Sale of Kinzie Park Condominium Units

The Company recognized a gain of \$2,156,000 during 2002 from the sale of residential condominiums in Chicago, Illinois.

Primestone Foreclosure and Impairment Losses

On September 28, 2000, the Company made a \$62,000,000 loan to Primestone Investment Partners, L.P. ("Primestone"). The Company received a 1% up-front fee and was entitled to receive certain other fees aggregating approximately 3% upon repayment of the loan. The loan bore interest at 16% per annum. Primestone defaulted on the repayment of this loan on October 25, 2001. The loan was subordinate to \$37,957,000 of other debt of the borrower that liened the Company's collateral. On October 31, 2001, the Company purchased the other debt for its face amount. The loans were secured by 7,944,893 partnership units in Prime Group Realty, L.P., the operating partnership of Prime Group Realty Trust (NYSE:PGE) and the partnership units are exchangeable for the same number of common shares of PGE. The loans are also guaranteed by affiliates of Primestone.

On November 19, 2001, the Company sold, pursuant to a participation agreement with a subsidiary of Cadim inc., a Canadian pension fund, a 50% participation in both loans at par for approximately \$50,000,000 reducing the Company's net investment in the loans at December 31, 2001 to \$56,768,000 including unpaid interest and fees of \$6,790,000. The participation did not meet the criteria for "sale accounting" under SFAS 140 because Cadim was not free to pledge or exchange the assets. Accordingly,

the Company was required to account for this transaction as a borrowing secured by the loan, rather than as a sale of the loan by classifying the participation as an “Other Liability” and continuing to report the outstanding loan balance at 100% in “Notes and Mortgage Loans Receivable” on the balance sheet.

Under the terms of the participation agreement, cash payments received shall be applied (i) first, to the reimbursement of reimbursable out-of-pocket costs and expenses incurred in connection with the servicing, administration or enforcement of the loans after November 19, 2001, and then to interest and fees owed to the Company through November 19, 2001, (ii) second, to the Company and Cadim, pro rata in proportion to the amount of interest and fees owed following November 19, 2001 and (iii) third, 50% to the Company and 50% to Cadim as recovery of principal.

On April 30, 2002, the Company and Cadim acquired the 7,944,893 partnership units at a foreclosure auction. The price paid for the units by application of a portion of Primestone’s indebtedness to the Company and Cadim was \$8.35 per unit, the April 30, 2002 closing price of shares of PGE on the New York Stock Exchange. On June 28, 2002, pursuant to the terms of the participation agreement, the Company transferred 3,972,447 of the partnership units to Cadim.

In the second quarter, in accordance with foreclosure accounting, the Company recorded a loss on the Primestone foreclosure of \$17,671,000 calculated based on (i) the acquisition price of the units and (ii) its valuation of the amounts realizable under the guarantees by affiliates of Primestone, as compared with the net carrying amount of the investment at April 30, 2002. In the third quarter of 2002, the Company recorded a \$2,229,000 write-down on its investment based on costs expended to realize the value of the guarantees. Further, in the fourth quarter of 2002, the Company recorded a \$15,857,000 write-down of its investment in Prime Group consisting of (i) \$14,857,000 to adjust the carrying amount of the Prime Group units to \$4.61 per unit, the closing price of PGE shares on December 31, 2002 on the New York Stock Exchange and (ii) \$1,000,000 for estimated costs to realize the value of the guarantees. The Company considered the decline in the value of the units which are convertible into stock to be other than temporary as of December 31, 2002, based on the fact that the market value of the units which are convertible into stock has been less than its cost for more than six months, the severity of the decline, market trends, the financial condition and near-term prospects of Prime Group and other relevant factors.

At December 31, 2002, the Company’s carrying amount of the investment was \$23,408,000, of which \$18,313,000 represents the carrying amount of the 3,972,447 partnership units owned by the Company (\$4.61 per unit), \$6,100,000 represents the amount expected to be realized under the guarantees, offset by \$1,005,000 representing the Company’s share of Prime Group Realty’s net loss through September 30, 2002 (see Note 4. Investments in and Advances to Partially-Owned Entities). Prior to April 30, 2002, this investment was in the form of a loan and was included in Notes and Mortgage Loans Receivable on the balance sheet.

At February 3, 2003, the closing price of PGE shares on the New York Stock Exchange was \$5.30 per share. The ultimate realization of the Company’s investment will depend upon the future performance of the Chicago real estate market and the performance of PGE, as well as the ultimate realizable value of the net assets supporting the guarantees and the Company’s ability to collect under the guarantees. In addition, the Company will continue to monitor this investment to determine whether additional write-downs are required based on (i) declines in value of the shares of PGE (for which the partnership units are exchangeable) which are “other than temporary” as used in accounting literature and (ii) the amount expected to be realized under the guarantees.

Vornado Realty Trust

Write-off Investments in Technology Companies

In the first quarter of 2001, the Company recorded a charge of \$4,723,000 resulting from the write-off of an equity investment in a technology company. In the second quarter of 2001, the Company recorded an additional charge of \$13,561,000 resulting from the write-off of all of its remaining equity investments in technology companies due to both the deterioration of the financial condition of these companies and the lack of acceptance by the market of certain of their products and services. In the fourth quarter of 2001, the Company recorded \$1,481,000 of income resulting from the reversal of a deferred liability relating to the termination of an agreement permitting one of the technology companies access to its properties.

Park Laurel Condominium Project

In the third quarter of 2001, the Park Laurel joint venture (69% interest owned by the Company) completed the sale of 52 condominium units of the total 53 units and received proceeds of \$139,548,000. The Company's share of the after-tax net gain was \$15,657,000. The Company's share of the after-tax net gain reflects \$3,953,000 (net of tax benefit of \$1,826,000) awards accrued under the venture's incentive compensation plan.

Write-off of Net Investment in RTR

In the third quarter of 2001, the Company wrote-off its entire net investment of \$7,374,000 in RTR based on the operating losses and an assessment of the value of the real estate.

Net Gains on Sale of Real Estate

On August 6, 2001, the Company sold its leasehold interest in 550/600 Mamaroneck Avenue for \$22,500,000, which approximated book value.

In September 1998, Atlantic City condemned the Company's property. In the third quarter of 1998, the Company recorded a gain of \$1,694,000, which reflected the condemnation award of \$3,100,000, net of the carrying value of the property of \$1,406,000. The Company appealed the amount and on June 27, 2001, was awarded an additional \$3,050,000, which has been recorded as a gain in the quarter ended June 30, 2001.

On May 17, 2001, the Company sold its 50% interest in 570 Lexington Avenue for \$60,000,000, resulting in a gain of \$12,445,000.

During 2000, the Company sold (i) its three shopping centers located in Texas for \$25,750,000, resulting in a gain of \$2,560,000 and (ii) its Westport, Connecticut office property for \$24,000,000, resulting in a gain of \$8,405,000.

4. INVESTMENTS IN PARTIALLY-OWNED ENTITIES

The Company's investments in partially-owned entities and income recognized from such investments is disclosed below. Summarized financial data is provided for (i) investments in entities which exceed 10% of the Company's total assets and (ii) investments in which the Company's share of partially-owned entities pre-tax income exceeds 10% of the Company's net income.

Balance Sheet Data:

(\$ in thousands)	Percentage Ownership	100% of These Entities							
		Company's Investment		Total Assets		Total Liabilities		Total Equity	
		2002	2001	2002	2001	2002	2001	2002	2001
Investments:									
Temperature Controlled Logistics	60%	\$448,295	\$ 474,862	\$1,347,382	\$1,379,212	\$ 584,510	\$ 610,727	\$731,240	\$ 768,485
Charles E. Smith Commercial Realty L.P. ⁽¹⁾	34%	— ⁽¹⁾	347,263	— ⁽¹⁾	\$1,308,297	— ⁽¹⁾	\$1,503,057	— ⁽¹⁾	\$(307,584)
Alexander's	33.1%	193,879	188,522	\$ 664,770	\$ 583,339	\$ 596,247	\$ 538,258	\$ 68,665	\$ 45,081
Newkirk Joint Ventures ⁽²⁾	21.7%	182,465	191,534	\$1,472,349	\$ 722,293	\$1,322,719	\$ 879,840	\$ 20,385	\$(157,547)
Partially-Owned Office Buildings ⁽⁴⁾	34%	29,421	23,346						
Starwood Ceruzzi Joint Venture	80%	24,959	25,791						
Monmouth Mall ⁽³⁾	50%	31,416	—						
Park Laurel	80%	3,481	(4,745) ⁽⁵⁾						
Prime Group Realty, L.P. and other guarantees	14.9%	23,408	—						
Other		60,387	23,622						
		\$997,711	\$1,270,195						

⁽¹⁾ Vornado owned a 34% interest in CESCO in 2001. On January 1, 2002, the Company acquired the remaining 66% of CESCO. See Note 3—“Acquisitions and Dispositions” for details of the acquisition.

⁽²⁾ The Company's investment in and advances to Newkirk Joint Ventures is comprised of:

	December 31, 2002	December 31, 2001
Investments in limited partnerships	\$134,200	\$143,269
Mortgages and loans receivable	39,511	39,511
Other	8,754	8,754
Total	\$182,465	\$191,534

On January 2, 2002, the Newkirk Joint Ventures' partnership interests were merged into a master limited partnership (the “MLP”) in which the Company has a 21.7% interest. In conjunction with the merger, the MLP completed a \$225,000 mortgage financing collateralized by its properties, subject to the existing first and certain second mortgages on those properties. The loan bears interest at LIBOR plus 5.5% with a LIBOR floor of 3% (8.5% at February 3, 2003) and matures on January 31, 2005, with two one-year extension options. As a result of the financing on February 6, 2002, the MLP repaid approximately \$28,200 of existing debt and distributed approximately \$37,000 to the Company. In 2003, the Company expects to receive distributions of approximately \$9,000 from the Newkirk MLP.

⁽³⁾ On October 10, 2002, a joint venture in which the Company owns a 50% interest acquired the Monmouth Mall. See Note 3—“Acquisitions and Dispositions” for further details.

⁽⁴⁾ As at December 31, 2002, includes a 20% interest in a property which was part of the CESCO acquisition in January 2002.

⁽⁵⁾ The credit balance at December 31, 2001, is a result of the accrual of awards under the ventures incentive compensation plan.

Vornado Realty Trust

Below is a summary of the debt of partially-owned entities as of December 31, 2002 and 2001, none of which is guaranteed by the Company.

(Amounts in thousands)	100% of Partially-Owned Entities Debt	
	December 31, 2002	December 31, 2001
Alexander's (33.1% interest) (see "Alexander's" on page 76 for further details):		
Term loan:		
Portion financed by the Company due on January 3, 2006 with interest at 12.48%	\$ 95,000	\$ 95,000
Portion financed by a bank, due March 15, 2003, with interest at LIBOR + 1.85% (repaid on July 3, 2002)	—	10,000
Line of Credit financed by the Company, due on January 3, 2006 with interest at 12.48% (prepayable without penalty)	24,000	24,000
Lexington Avenue construction loan payable, due on January 3, 2006, plus two one-year extensions, with interest at LIBOR plus 2.50% (3.88% at December 31, 2002)	55,500	—
Rego Park mortgage payable, due in June 2009, with interest at 7.25%	82,000	82,000
Kings Plaza Regional Shopping Center mortgage payable, due in June 2011, with interest at 7.46% (prepayable with yield maintenance)	219,308	221,831
Paramus mortgage payable, due in October 2011, with interest at 5.92% (prepayable without penalty)	68,000	68,000
Other notes and mortgages payable (repaid on July 3, 2002)	—	15,000
Temperature Controlled Logistics (60% interest):		
Mortgage notes payable collateralized by 58 temperature controlled warehouses, due in May 2008, requires amortization based on a 25 year term with interest at 6.94% (prepayable with yield maintenance)	537,716	563,782
Other notes and mortgages payable	37,789	38,748
Newkirk Joint Ventures (21.7% interest):		
Portion of first mortgages and contract rights, collateralized by the partnerships' real estate, due from 2002 to 2024, with a weighted average interest rate of 10.62% at December 31, 2002 (various prepayment rights)	1,432,438	1,336,989
Charles E. Smith Commercial Realty L.P. (34% interest in 2001):		
29 mortgages payable	—	1,470,057
Prime Group Realty L.P. (14.9% interest) ⁽¹⁾ :		
24 mortgages payable	868,374	—
Partially-Owned Office Buildings:		
330 Madison Avenue (25% interest) mortgage note payable, due in April 2008, with interest at 6.52% (prepayable with yield maintenance)	60,000	60,000
Fairfax Square (20% interest) mortgage note payable due in August 2009, with interest at 7.50%	68,900	—
825 Seventh Avenue (50% interest) mortgage payable, due in October 2014, with interest at 8.07% (prepayable with yield maintenance)	23,295	23,552
Orleans Hubbard (50% interest) mortgage note payable, due in March 2009, with interest at 7.03%	9,961	—
Wells/Kinzie Garage (50% interest) mortgage note payable, due in May 2009, with interest at 7.03%	15,860	—
Monmouth Mall (50% interest):		
Mortgage note payable, due in November 2005, with interest at LIBOR + 2.05% (3.49% at December 31, 2002)	135,000	—
Las Catalinas Mall (50% interest):		
Mortgage notes payable ⁽²⁾	—	68,591
Russian Tea Room (50% interest) mortgages payable ⁽³⁾	—	13,000

Based on the Company's ownership interest in the partially-owned entities above, the Company's share of the debt of these partially-owned entities was \$1,048,108,000 and \$1,319,535,000 as of December 31, 2002 and 2001.

⁽¹⁾ Balance as of September 30, 2002, as Prime Group's annual report on Form 10-K for the year ended December 31, 2002, has not been filed prior to the filing of this annual report on Form 10-K.

⁽²⁾ The Company increased its interest in Las Catalinas to 100% on September 23, 2002. Accordingly, Las Catalinas is consolidated as of September 30, 2002.

⁽³⁾ On November 18, 2002 the Russian Tea Room mortgage loans were repaid with proceeds from the sale of the property.

Income Statement Data:

(\$ in thousands)	Company's Income from Partially Owned Entities			100% of These Entities					
				Total Revenues			Net Income (loss)		
	2002	2001	2000	2002	2001	2000	2002	2001	2000
Alexander's:									
Equity in income ⁽¹⁾	\$ 7,556	\$ 8,465	\$ 1,105	\$ 76,193	\$ 69,343	\$ 63,965	\$ 23,584	\$ 27,386	\$ 5,197
Interest income ⁽²⁾	10,401	11,899	11,948						
Development and guarantee fees ⁽²⁾	6,915	—	—						
Management and leasing fee income ⁽¹⁾	4,781	5,354	4,310						
	\$29,653	\$25,718	\$17,363						
Temperature Controlled Logistics:									
Equity in net income (loss)	\$ 4,144	\$12,093	\$23,244	\$117,663	\$126,957	\$154,341	\$(20,231)	\$16,647	\$37,284
Management fees	5,563	5,354	5,534						
	9,707	17,447	28,778						
CESCR ⁽³⁾	—	28,653	25,724	— ⁽³⁾	\$382,502	\$344,084	— ⁽³⁾	\$82,713	\$76,707
Newkirk MLP:									
Equity in income	26,499	25,470	18,632	\$295,369	\$179,551	—	\$121,860	\$84,900	—
Interest and other income	8,001	5,474	5,894						
Partially-Owned Office Buildings ⁽⁴⁾									
Monmouth Mall	1,966	4,093	2,832						
Prime Group Realty LP ⁽⁵⁾	1,022	—	—						
Other	(1,005)	—	—						
	(1,732)	(525)	4,794						
	\$ 44,458	\$80,612	\$86,654						

⁽¹⁾ Equity in income in 2002 includes the Company's \$3,524 share of Alexander's gain on sale of its Third Avenue property. Equity in income in 2001 includes (i) the Company's \$6,298 share of Alexander's gain on sale of its Fordham Road property, (ii) a charge of \$1,684 representing the Company's share of abandoned development costs and (iii) \$1,170 representing the Company's share of Alexander's gain on the early extinguishment of debt on its Fordham Road property. Management and leasing fee income include fees of \$350 and \$520 paid to the Company in 2002 and 2001 in connection with sales of real estate.

⁽²⁾ Alexander's capitalizes the fees and interest charged by the Company. Because the Company owns 33.1% of Alexander's, the Company recognizes 66.9% of such amounts as income and the remainder is reflected as a reduction of the Company's carrying amount of the investment in Alexander's.

⁽³⁾ The Company owned a 34% interest in CESCR. On January 1, 2002, the Company acquired the remaining 66% of CESCR it did not previously own. Accordingly, CESCR is consolidated as of January 1, 2002.

⁽⁴⁾ Represents the Company's interests in 330 Madison Avenue (24.8%), 825 Seventh Avenue (50%) and 570 Lexington Avenue (50%). On May 17, 2001, the Company sold its 50% interest in 570 Lexington Avenue for \$60,000, resulting in a gain of \$12,445, which is not included in income in the table above.

⁽⁵⁾ Represents the Company's share of net loss for the period from April 30, 2002 (date of acquisition) to September 30, 2002, which includes (i) a loss of \$357 from discontinued operations and (ii) a loss of \$147 from the sale of real estate. The Company's share of equity in income or loss for the period from October 1, 2002 to December 31, 2002 will be recognized in earnings in the quarter ended March 31, 2003, as the investee has not released its earnings for the year ended December 31, 2002 prior to the filing of the Company's annual report on Form 10-K.

Vornado Realty Trust

Alexander's

Ownership

The Company owns 1,655,000 common shares or 33.1% of the outstanding common stock of Alexander's at December 31, 2002. Alexander's is managed by and its properties are leased and developed by the Company pursuant to management, leasing and development agreements with one-year terms expiring in March of each year, which are automatically renewable. In conjunction with the closing of the Alexander's Lexington Avenue construction loan on July 3, 2002, these agreements were revised to cover the Alexander's Lexington Avenue property separately. Further, the Lexington Avenue management and development agreements were amended to provide for a term lasting until substantial completion of the development of the property, with automatic renewals, and for the payment of the development fee upon the earlier of January 3, 2006, or the payment in full of the construction loan encumbering the property. The Company is entitled to a development fee estimated to be approximately \$26,300,000, based on 6% of construction costs, as defined, of which \$7,667,000 has been recognized as income during the year ended December 31, 2002.

Debt

At December 31, 2002, the Company had loans receivable from Alexander's of \$119,000,000, including \$24,000,000 drawn under the \$50,000,000 line of credit the Company granted to Alexander's on August 1, 2000. The maturity date of the loan and the line of credit is the earlier of January 3, 2006 or the date the Alexander's Lexington Avenue construction loan is repaid. The interest rate on the loan and line of credit, which resets quarterly using the same spread to treasuries as presently exists with a 3% floor for treasuries, is 12.48% at December 31, 2002. The Company believes that although Alexander's has disclosed that it does not have positive cash flow sufficient to repay this loan to the Company currently, Alexander's will be able to repay the loan upon the successful development and permanent financing of its Lexington Avenue development project or through asset sales.

On July 3, 2002, Alexander's finalized a \$490,000,000 loan with HVB Real Estate Capital (HYPO Vereinsbank) to finance the construction of its approximately 1.3 million square foot multi-use building at its 59th Street and Lexington Avenue location. The estimated construction costs in excess of the construction loan of approximately \$140,000,000 will be provided by Alexander's. The loan has an interest rate of LIBOR plus 2.5% and a term of forty-two months plus two one-year extensions. Alexander's has received an initial funding of \$55,500,000 under the loan of which \$25,000,000 was used to repay existing loans and notes payable. Pursuant to this loan, Vornado has agreed to guarantee, among other things, the lien free, timely completion of the construction of the project and funding of project costs in excess of a stated budget, as defined in the loan agreement, if not funded by Alexander's (the "Completion Guarantee"). The \$6,300,000 estimated fee payable by Alexander's to the Company for the Completion Guarantee is 1% of construction costs (as defined) and is payable at the same time that the development fee is payable. In addition, if the Company should advance any funds under the Completion Guarantee in excess of the \$26,000,000 currently available under the secured line of credit, interest on those advances is at 15% per annum.

Agreements with Alexander's

Alexander's is managed by and its properties are leased by the Company, pursuant to agreements with a one-year term expiring in March of each year which are automatically renewable. The annual management fee payable to the Company by Alexander's is equal to the sum of (i) \$3,000,000, (ii) 3% of the

gross income from the Kings Plaza Mall, and (iii) 6% of development costs with minimum guaranteed fees of \$750,000 per annum.

The leasing agreement provides for the Company to generally receive a fee of (i) 3% of sales proceeds and (ii) 3% of lease rent for the first ten years of a lease term, 2% of lease rent for the eleventh through the twentieth years of a lease term and 1% of lease rent for the twenty-first through thirtieth year of a lease term, subject to the payment of rents by Alexander's tenants. Such amount is receivable annually in an amount not to exceed \$2,500,000 until the present value of such installments (calculated at a discount rate of 9% per annum) equals the amount that would have been paid at the time the transactions which gave rise to the commissions occurred. At December 31, 2002, \$410,000 is due to the Company under this agreement.

Other

The Company constructed a \$16.3 million community facility and low-income residential housing development (the "30th Street Venture"), in order to receive 163,728 square feet of transferable development rights, generally referred to as "air rights." The Company donated the building to a charitable organization. The Company sold 106,796 square feet of these air rights to third parties at an average price of \$120 per square foot. An additional 28,821 square feet of air rights was sold to Alexander's at a price of \$120 per square foot for use at Alexander's 59th Street development project (the "59th Street Project"). In each case, the Company received cash in exchange for air rights. The Company identified third party buyers for the remaining 28,111 square feet of air rights related to the 30th Street Venture. These third party buyers wanted to use the air rights for the development of two projects located in the general area of 86th Street which was not within the required geographical radius of the construction site nor in the same Community Board as the low-income housing and community facility project. The 30th Street Venture asked Alexander's to sell 28,111 square feet of the air rights it already owned to the third party buyers (who could use them) and the 30th Street Venture would replace them with 28,111 square feet of air rights. In October 2002, the Company sold 28,111 square feet of air rights to Alexander's for an aggregate sales price of \$3,059,000 (an average of \$109 per square foot). Alexander's then sold an equal amount of air rights to the third party buyers for an aggregate sales price of \$3,339,000 (an average of \$119 per square foot).

On October 5, 2001, Alexander's entered into a ground lease for its Paramus, N.J. property with IKEA Property, Inc. The lease has a 40-year term with an option to purchase at the end of the 20th year for \$75,000,000. Further, Alexander's has obtained a \$68,000,000 interest only, non-recourse mortgage loan on the property from a third party lender. The interest rate on the debt is 5.92% with interest payable monthly until maturity in October 2011. The triple net rent each year is the sum of \$700,000 plus the amount of debt service on the mortgage loan. If the purchase option is not exercised at the end of the 20th year, the triple net rent for the last 20 years must include debt service sufficient to fully amortize the \$68,000,000 over the remaining 20-year lease period.

On May 1, 2001 Alexander's entered into a lease agreement with Bloomberg L.P., for approximately 695,000 square feet of office space. The initial term of the lease is for 25 years, with one ten-year renewal option. Base annual net rent is \$34,529,000 in each of the first four years and \$38,533,000 in the fifth year with similar percentage increases each four years. There can be no assurance that this project ultimately will be completed, completed on time or completed for the budgeted amount. If the project is not completed on a timely basis, the lease may be cancelled and significant penalties may apply.

Vornado Realty Trust

On August 30, 2002, Alexander's sold its Third Avenue property, located in the Bronx, New York, which resulted in a gain of \$10,366,000. On January 12, 2001, Alexander's sold its Fordham Road property located in the Bronx, New York, for \$25,500,000, which resulted in a gain of \$19,026,000. In addition, Alexander's paid off the mortgage on its Fordham Road property at a discount, which resulted in a gain from early extinguishment of debt of \$3,534,000 in the first quarter of 2001.

5. NOTES AND MORTGAGE LOANS RECEIVABLE

Loan to Commonwealth Atlantic Properties ("CAPI")

On March 4, 1999 the Company made an additional \$242,000,000 investment in Charles E. Smith Commercial Realty L.P. ("CESCR") by contributing to CESCR the land under certain CESCR office properties in Crystal City, Arlington, Virginia and partnership interests in certain CESCR subsidiaries. The Company acquired these assets from Commonwealth Atlantic Properties, Inc. ("CAPI"), an affiliate of Lazard Freres Real Estate Investors L.L.C., for \$242,000,000, immediately prior to the contribution to CESCR. In addition, the Company acquired from CAPI for \$8 million the land under a Marriott Hotel located in Crystal City. The Company paid the \$250,000,000 purchase price to CAPI by issuing 4,998,000 of the Company's Series E-1 convertible preferred units. In connection with these transactions, the Company agreed to make a five-year \$41,200,000 loan to CAPI with interest at 8%, increasing to 9% ratably over the term. The loan is secured by approximately 1.1 million of the Company's Series E-1 convertible preferred units issued to CAPI. Each Series E-1 convertible preferred unit is convertible into 1.1364 of the Company's common shares. The total value of these units, on an as-converted basis, was \$46,500,000 based on a closing price of \$37.20 per common share on December 31, 2002.

Loan to Vornado Operating Company ("Vornado Operating")

At December 31, 2002, the amount outstanding under the revolving credit agreement with Vornado Operating was \$21,989,000. Vornado Operating has disclosed that in the aggregate its investments do not, and for the foreseeable future are not expected to, generate sufficient cash flow to pay all of its debts and expenses. Further, Vornado Operating states that its only investee, AmeriCold Logistics ("Tenant"), anticipates that its Landlord, a partnership 60% owned by the Company and 40% owned by Crescent Real Estate Equities, will need to restructure the leases between the Landlord and the Tenant to provide additional cash flow to the Tenant (the Landlord has previously restructured the leases to provide additional cash flow to the Tenant). Management anticipates a further lease restructuring and the sale and/or financing of assets by AmeriCold Logistics, and accordingly, Vornado Operating is expected to have a source to repay the debt under this facility, which may be extended. Since January 1, 2002, the Company has not recognized interest income on the debt under this facility. The Company has assessed the collectibility of this loan as of December 31, 2002 and determined that it is not impaired.

Dearborn Center Mezzanine Construction Loan

As of December 31, 2002, \$60,758,000 is outstanding under the Dearborn Center Mezzanine Construction Loan to a special purpose entity, of which \$23,392,000 has been funded by the Company, representing a 38.5% interest. The special purpose entity's sole asset is Dearborn Center, a 1.5 million square foot high-rise office tower under construction in Chicago. The entity is owned by Prime Group Realty L.P. and another investor. The Company is a member of a loan syndicate led by a money center bank. The proceeds of the loan are being used to finance the construction, and are subordinate to a \$225,000,000 first mortgage. The loan is due January 21, 2004, three years from the date of the initial draw, and provides for a 1-year extension at the borrower's option (assuming net operating income at a specified level and a cash reserve sufficient to fund interest for the extension period). The loan bears interest at 12% per annum plus additional interest upon repayment ranging from a minimum of 9.5% to 11.5%.

6. DEBT

Following is a summary of the Company's debt:

(Amounts in thousands)	Maturity	Interest Rate as at December 31, 2002	Balance as of	
			December 31, 2002	December 31, 2001
Notes and Mortgages Payable:				
Fixed Interest:				
Office:				
NYC Office:				
Two Penn Plaza	03/04	7.08%	\$ 154,669	\$ 157,697
888 Seventh Avenue ⁽¹⁾	02/06	6.63%	105,000	105,000
Eleven Penn Plaza	05/07	8.39%	50,383	51,376
866 UN Plaza	04/04	7.79%	33,000	33,000
CESCR Office: ⁽²⁾				
Crystal Park 1-5	07/06-08/13	6.66%-8.39%	264,441	— ⁽²⁾
Crystal Gateway 1-4				
Crystal Square 5	07/12-01/25	6.75%-7.09%	215,978	— ⁽²⁾
Crystal Square 2, 3 and 4	10/10-11/14	7.08%-7.14%	146,081	— ⁽²⁾
Skyline Place	08/06-12/09	6.6%-6.93 %	139,212	— ⁽²⁾
1101 17th, 1140 Connecticut, 1730 M & 1150 17th	08/10	6.74%	97,318	— ⁽²⁾
Courthouse Plaza 1 and 2	01/08	7.05%	80,062	— ⁽²⁾
Crystal Gateway N., Arlington Plaza and 1919 S. Eads	11/07	6.77%	72,721	— ⁽²⁾
Reston Executive I, II & III	01/06	6.75%	73,844	— ⁽²⁾
Crystal Plaza 1-6	10/04	6.65%	70,356	— ⁽²⁾
One Skyline Tower	06/08	7.12%	65,764	— ⁽²⁾
Crystal Malls 1-4	12/11	6.91%	65,877	— ⁽²⁾
1750 Pennsylvania Avenue	06/12	7.26%	49,794	— ⁽²⁾
One Democracy Plaza	02/05	6.75%	27,640	— ⁽²⁾
Retail:				
Cross collateralized mortgages payable on 42 shopping centers	03/10	7.93%	487,246	492,156
Green Acres Mall	02/08	6.75%	150,717	152,894
Montehiedra Town Center	05/07	8.23%	59,638	60,359
Las Catalinas Mall ⁽³⁾	11/13	6.97%	67,692	—
Merchandise Mart:				
Market Square Complex ⁽⁴⁾	07/11	7.95%	48,213	49,702
Washington Design Center ⁽⁵⁾	10/11	6.95%	48,542	48,959
Washington Office Center	02/04	6.80%	44,924	46,572
Other	10/10-06/13	7.52%-7.71%	18,703	18,951
Other:				
Industrial Warehouses ⁽⁶⁾	10/11	6.95%	49,423	50,000
Student Housing Complex	11/07	7.45%	19,019	19,243
Other	08/21	9.90%	6,937	8,659
Total Fixed Interest Notes and Mortgages Payable		7.17%	2,713,194	1,294,568

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *continued*

Vornado Realty Trust

(Amounts in thousands)	Maturity	Spread over LIBOR	Interest Rate		Balance as of	
			as at December 31, 2002	December 31, 2002	December 31, 2001	
Notes and Mortgages Payable:						
Variable Interest:						
Office:						
NYC Office:						
One Penn Plaza ⁽⁷⁾	06/05	L+125	2.67%	\$ 275,000	\$ 275,000	
770 Broadway/595 Madison Avenue cross-collateralized mortgage ⁽⁸⁾	04/03	L+40	1.78%	153,659	123,500	
909 Third Avenue	08/03	L+165	3.09%	105,837	105,253	
Two Park Avenue ⁽⁹⁾	03/03	L+145	—	—	90,000	
CESCR Office:						
Tyson Dulles Plaza	06/03	L+130	2.72%	69,507	— ⁽²⁾	
Commerce Executive III, IV & V	07/03	L+150	2.92%	53,307	— ⁽²⁾	
Merchandise Mart:						
Merchandise Mart ⁽⁹⁾	10/02	L+150	—	—	250,000	
Furniture Plaza	02/03	L+200	3.44%	48,290	43,524	
33 North Dearborn Street	09/03	L+175	3.13%	18,926	19,000	
350 North Orleans ⁽⁹⁾	06/02	L+165	—	—	70,000	
Other	01/03	Prime-50	3.75%	—	294	
Other:						
Palisades construction loan	02/04	L+185	3.17%	100,000	90,526	
Hotel Pennsylvania	10/02	L+160	—	—	115,508	
Total Variable Interest Notes and Mortgages Payable			3.07%	824,526	1,182,605	
Total Notes and Mortgages Payable				\$3,537,720	\$ 2,477,173	
Senior unsecured debt due 2007 at fair value (\$34,245 in excess of accreted note balance)⁽⁹⁾						
	06/07	L+77	2.15 %	\$ 533,600	\$ —	
Unsecured revolving credit facility						
	07/03	L+90	—	\$ —	\$ —	

⁽¹⁾ On January 11, 2001, the Company completed a \$105,000 refinancing of its 888 Seventh Avenue office building. The loan bears interest at a fixed rate of 6.63% and matures on February 1, 2006. A portion of the proceeds received was used to repay the then existing mortgage of \$55,000.

⁽²⁾ On January 1, 2002, the Company acquired the remaining 66% of CESCR it did not previously own. Prior to January 1, 2002, the Company's share of CESCR's debt was included in Investments in and Advances to Partially-Owned Entities. In connection with the acquisition, CESCR's fixed rate debt of \$1,282,780 was fair valued at \$1,317,428 under purchase accounting.

⁽³⁾ On September 23, 2002, the Company acquired the 50% of the Mall and the 25% of Kmart's anchor store it did not already own. Prior to this date, the Company accounted for its investment on the equity method and the Company's share of the debt was included in Investments in and Advances to Partially-Owned Entities.

⁽⁴⁾ On July 11, 2001, the Company completed a \$50,000 refinancing of its Market Square Complex. The loan bears interest at a fixed rate of 7.95% per annum and matures in July 2011. The proceeds received were used to repay the then existing mortgage of \$49,000.

⁽⁵⁾ On October 16, 2001, the Company completed a \$49,000 refinancing of its Washington Design Center property. The loan bears interest at a fixed rate of 6.95% and matures on October 16, 2011. A portion of the proceeds received was used to repay the then existing mortgage of \$23,000.

⁽⁶⁾ On September 20, 2001, the Company completed a \$50,000 mortgage financing, cross collateralized by its eight industrial warehouse properties. The loan bears interest at a fixed rate of 6.95% per annum and matures on October 1, 2011.

⁽⁷⁾ On June 21, 2002, one of the lenders purchased the other participant's interest in the loan. At the same time, the loan was extended for one year, with certain modifications including, (i) making the risk of a loss due to terrorism (as defined) not covered by insurance recourse to the Company and (ii) the granting of two 1-year renewal options to the Company.

⁽⁸⁾ On April 1, 2002, the Company increased its mortgage financing cross collateralized by its 770 Broadway/595 Madison Avenue properties by \$115,000. On July 15, 2002, the Company repaid \$84,841 with proceeds received from a third party which resulted in a gain on transfer of mortgages of \$2,096. The proceeds of the loan are in a restricted mortgage escrow account which bears interest at the same rate as the loan, and at December 31, 2002 totals \$153,659.

⁽⁹⁾ On June 24, 2002, the Company completed an offering of \$500,000 aggregate principal amount of 5.625% senior unsecured notes due June 15, 2007. Interest on the notes is payable semi-annually on June 15th and December 15th, commencing December 15, 2002. The notes were priced at 99.856% of their face amount to yield 5.659%. The net proceeds of approximately \$496,300 were used to repay the mortgage payable on 350 North Orleans, Two Park Avenue, the Merchandise Mart and Seven Skyline. On June 27, 2002, the Company entered into interest rate swaps that effectively converted the interest rate on the \$500,000 senior unsecured notes due 2007 from a fixed rate of 5.625% to a floating rate of LIBOR plus .7725%, based upon the trailing 3 month LIBOR rate (2.15% if set on December 31, 2002). As a result of the hedge accounting for the interest rate swap on the Company's senior unsecured debt, the Company recorded a fair value adjustment of \$34,245, as of December 31, 2002 which is equal to the fair value of the interest rate swap asset.

The net carrying amount of properties collateralizing the notes and mortgages amounted to \$4,938,012,000 at December 31, 2002. As at December 31, 2002, the principal repayments for the next five years and thereafter are as follows:

(\$ in thousands)	
Year Ending December 31,	Amount
2003	\$ 449,526 ⁽¹⁾
2004	402,949
2005	302,640
2006	261,385
2007	822,536
Thereafter	1,832,284

⁽¹⁾ Includes \$153,659 which is offset by an equivalent amount of cash held in a restricted mortgage escrow account.

The Company's debt instruments, consisting of mortgage loans secured by its properties (which are generally non-recourse to the Company), its revolving credit agreement and its senior unsecured notes due 2007, contain customary covenants requiring the Company to maintain insurance. There can be no assurance that the lenders under these instruments will not take the position that an exclusion from all risk insurance coverage for losses due to terrorist acts is a breach of these debt instruments that allows the lenders to declare an event of default and accelerate repayment of debt. The Company has received correspondence from four lenders regarding terrorism insurance coverage, to which the Company has responded. In these letters the lenders took the position that under the agreements governing the loans provided by these lenders the Company was required to maintain terrorism insurance on the properties securing the various loans. The aggregate amount of borrowings under these loans as of December 31, 2002 was approximately \$770.4 million, and there was no additional borrowing capacity. Subsequently, the Company obtained an aggregate of \$360 million of separate coverage for "terrorist acts". To date, one of the lenders has acknowledged to the Company that it will not raise any further questions based on the Company's terrorism insurance coverage in place, and the other three lenders have not raised any further questions regarding the Company's insurance coverage. If lenders insist on greater coverage for these risks, it could adversely affect the Company's ability to finance and/or refinance its properties and to expand its portfolio.

7. SHAREHOLDERS' EQUITY

During the three years ended December 31, 2002, the Company sold 11,173,743 common shares. The following are the details of the sales.

Vornado Realty Trust

Sale and Issuance of Common Shares

On February 25, 2002, the Company sold 1,398,743 common shares based on the closing price of \$42.96 on the NYSE. The net proceeds to the Company were approximately \$56,453,000.

On November 19, 2001, the Company sold 9,775,000 common shares pursuant to an effective registration statement based on the closing price of \$40.58 on the NYSE. The net proceeds to the Company were approximately \$377,200,000. In connection therewith the Company repaid the \$285,000,000 then outstanding under its revolving credit facility.

\$3.25 Series A Preferred Shares of Beneficial Interest

Holders of Series A Preferred Shares of beneficial interest are entitled to receive dividends in an amount equivalent to \$3.25 per annum per share. These dividends are cumulative and payable quarterly in arrears. The Series A Preferred Shares are convertible at any time at the option of their respective holders at a conversion rate of 1.38504 common shares per Series A Preferred Share, subject to adjustment in certain circumstances. In addition, upon the satisfaction of certain conditions the Company, at its option, may redeem the \$3.25 Series A Preferred Shares at a current conversion rate of 1.38504 common shares per Series A Preferred Share, subject to adjustment in certain circumstances. At no time will the Series A Preferred Shares be redeemable for cash.

Series B Preferred Shares of Beneficial Interest

Holders of Series B Preferred Shares of beneficial interest are entitled to receive dividends at an annual rate of 8.5% of the liquidation preference, or \$2.125 per Series B Preferred Share per annum. These dividends are cumulative and payable quarterly in arrears. The Series B Preferred Shares are not convertible into or exchangeable for any other property or any other securities of the Company at the election of the holders. However, subject to certain limitations relating to the source of funds used in connection with any such redemption, on or after March 17, 2004 (or sooner under limited circumstances), the Company, at its option, may redeem Series B Preferred Shares at a redemption price of \$25.00 per share, plus any accrued and unpaid dividends through the date of redemption. The Series B Preferred Shares have no maturity date and will remain outstanding indefinitely unless redeemed by the Company.

Series C Preferred Shares of Beneficial Interest

Holders of Series C Preferred Shares of beneficial interest are entitled to receive dividends at an annual rate of 8.5% of the liquidation preference, or \$2.125 per Series C Preferred Share per annum. These dividends are cumulative and payable quarterly in arrears. The Series C Preferred Shares are not convertible into or exchangeable for any other property or any other securities of the Company at the election of the holders. However, subject to certain limitations relating to the source of funds used in connection with any such redemption, on or after May 17, 2004 (or sooner under limited circumstances), the Company, at its option, may redeem Series C Preferred Shares at a redemption price of \$25.00 per share, plus any accrued and unpaid dividends through the date of redemption. The Series C Preferred Shares have no maturity date and will remain outstanding indefinitely unless redeemed by the Company.

8. EMPLOYEES' SHARE OPTION PLAN

The Company grants various officers and employees incentive share options and non-qualified options to purchase common shares. Options granted are at prices equal to 100% of the market price of the

Company's shares at the date of grant. Shares vest on a graduated basis, becoming fully vested 36 months after grant. All options expire ten years after grant.

The Plan also provides for the award of Stock Appreciation Rights, Performance Shares and Restricted Stock, as defined. As of December 31, 2002, there were 250,927 restricted shares or rights to receive restricted shares outstanding, excluding 626,566 shares issued to the Company's President in connection with his employment agreement.

In 2002 and prior years, the Company accounted for stock-based compensation using the intrinsic value method. Accordingly, no stock-based compensation was recognized in the Company's financial statements for these years. If compensation cost for Plan awards had been determined based on fair value at the grant dates, net income and income per share would have been reduced to the pro-forma amounts below, for the years ended December 31, 2002, 2001, and 2000:

(Amounts in thousands, except share and per-share amounts)	December 31, 2002	December 31, 2001	December 31, 2000
Net income applicable to common shares:			
As reported	\$ 209,736	\$ 227,233	\$ 195,301
Stock-based compensation cost, net of minority interest	8,092	10,606	14,465
Pro forma	\$ 201,644	\$ 216,627	\$ 180,836
Net income per share applicable to common shares:			
Basic:			
As reported	\$ 1.98	\$ 2.55	\$ 2.26
Pro forma	1.90	2.43	2.09
Diluted:			
As reported	\$ 1.91	\$ 2.47	\$ 2.20
Pro forma	1.84	2.35	2.04

The fair value of each option grant is estimated on the date of grant using an option-pricing model with the following weighted-average assumptions used for grants in the periods ending December 31, 2002, 2001 and 2000.

	December 31, 2002	December 31, 2001	December 31, 2000
Expected volatility	17%	17%	17%
Expected life	5 years	5 years	5 years
Risk-free interest rate	3.0%	4.38%	5.0%
Expected dividend yield	6.0%	6.0%	6.0%

Vornado Realty Trust

A summary of the Plan's status and changes during the years then ended, is presented below:

	2002		2001		2000	
	Shares	Weighted-Average Exercise Price	Shares	Weighted-Average Exercise Price	Shares	Weighted-Average Exercise Price
Outstanding at January 1	15,453,100	\$ 32.25	15,861,260	\$ 32.25	11,472,352	\$ 32.65
Granted	3,655,500	42.14	26,000	35.88	4,863,750	31.02
Exercised	(114,181)	28.17	(314,965)	31.91	(377,440)	26.29
Cancelled	(198,053)	39.64	(119,195)	34.12	(97,402)	34.86
Outstanding at December 31	18,796,366	34.60	15,453,100	32.25	15,861,260	32.26
Options exercisable at December 31	13,674,177	\$ 33.00	11,334,124		7,272,878	
Weighted-average fair value of options granted during the year ended December 31 (per option)	\$ 3.06		\$ 3.46		\$ 2.98	

The following table summarizes information about options outstanding under the Plan at December 31, 2002:

Range of Exercise Price	Options Outstanding			Options Exercisable	
	Number Outstanding at December 31, 2002	Weighted-Average Remaining Contractual Life	Weighted-Average Exercise Price	Number Exercisable at December 31, 2002	Weighted-Average Exercise Price
\$ 0-\$12	26,308	0.1 Years	\$ 11.42	26,308	\$ 11.42
\$12-\$19	74,500	2.3 Years	\$ 17.89	74,500	\$ 17.89
\$19-\$24	3,500,000	3.9 Years	\$ 23.47	3,500,000	\$ 23.47
\$24-\$27	149,570	4.1 Years	\$ 26.28	149,570	\$ 26.28
\$27-\$32	4,969,502	6.7 Years	\$ 30.72	3,543,983	\$ 30.70
\$32-\$36	2,856,725	6.1 Years	\$ 33.68	2,772,740	\$ 33.65
\$36-\$40	211,170	4.8 Years	\$ 38.92	204,735	\$ 39.00
\$40-\$44	4,235,591	8.7 Years	\$ 42.26	664,341	\$ 43.05
\$44-\$46	2,508,000	5.0 Years	\$ 45.31	2,473,000	\$ 45.31
\$46-\$49	265,000	5.1 Years	\$ 48.41	265,000	\$ 48.41
\$ 0-\$49	18,796,366	6.2 Years	\$ 34.60	13,674,177	\$ 33.00

Shares available for future grant under the Plan at December 31, 2002 were 9,963,500, of which 2,500,000 are subject to shareholder approval.

9. RETIREMENT PLAN

In December 1997, benefits under the Company's Retirement Plan were frozen. Prior to December 31, 1997, the Company's qualified plan covered all full-time employees. The Plan provided annual pension benefits that were equal to 1% of the employee's annual compensation for each year of participation. The funding policy is in accordance with the minimum funding requirements of ERISA.

Pension expense includes the following components:

(Amounts in thousands, except percentages)	Year Ended December 31,		
	2002	2001	2000
Interest cost on projected benefit obligation	\$ 587	\$ 565	\$ 567
Expected return on assets	(235)	(412)	(374)
Net amortization and deferral	(56)	32	30
Net pension expense	\$ 296	\$ 185	\$ 223

Assumptions used in determining the net pension expense:

Discount rate	6.25%	7.25%	7.75%
Rate of increase in compensation levels	—*	—*	—*
Expected rate of return on assets	7.00%	7.00%	7.00%

*Not applicable, as benefits under the Plan were frozen in December 1997.

The following table sets forth the Plan's funded status and the amount recognized in the Company's balance sheet:

(\$ in thousands)	Year Ended December 31,		
	2002	2001	2000
Change in benefit obligation			
Benefit obligation at beginning of year	\$ 7,950	\$ 7,530	\$ 7,918
Interest cost	587	565	567
Benefit payments	(970)	(793)	(637)
Experience loss/(gain)	1,451	648	(318)
Benefit obligation at end of year	9,018	7,950	7,530
Change in plan assets			
Fair value of plan assets at beginning of year	6,056	5,732	5,284
Employer contribution	667	821	698
Benefit payments	(970)	(793)	(637)
Actual return on assets	235	295	387
Fair value of plan assets at end of year	5,988	6,055	5,732
Funded status	(3,030)	(1,895)	(1,798)
Unrecognized loss	3,517	2,011	1,279
Net Amount Recognized	\$ 487	\$ 116	\$ (519)

Amounts recognized in the consolidated balance sheets consist of:

Accrued benefit liability	\$ (3,030)	\$ (1,895)	\$ (1,798)
Accumulated other comprehensive loss	3,517	2,011	1,279
Net amount recognized	\$ 487	\$ 116	\$ (519)

Plan assets are invested in U.S. government obligations and securities backed by U.S. government guaranteed mortgages.

Vornado Realty Trust

10. LEASES

As lessor:

The Company leases space to tenants in office buildings and shopping centers under operating leases. Most of the leases provide for the payment of fixed base rentals payable monthly in advance. Shopping center leases provide for the pass-through to tenants of real estate taxes, insurance and maintenance. Office building leases generally require the tenants to reimburse the Company for operating costs and real estate taxes above their base year costs. Shopping center leases also provide for the payment by the lessee of additional rent based on a percentage of the tenants' sales. As of December 31, 2002, future base rental revenue under non-cancelable operating leases, excluding rents for leases with an original term of less than one year and rents resulting from the exercise of renewal options, is as follows:

(\$ in thousands)	
Year Ending December 31:	Amount
2003	\$1,078,251
2004	980,075
2005	856,829
2006	755,350
2007	679,393
Thereafter	3,427,665

These amounts do not include rentals based on tenants' sales. These percentage rents approximated \$1,832,000, \$2,157,000, and \$4,825,000 for the years ended December 31, 2002, 2001, and 2000.

Former Bradlees Locations

The Company previously leased 18 locations to Bradlees which closed all of its stores in February 2001. The Company has re-leased nine of the former Bradlees locations; three to Kohl's, two each to Lowe's and Haynes Furniture, and one each to Home Depot and Wal-Mart. Lowe's and Wal-Mart will construct their own stores, subject to the receipt of various governmental approvals and the relocation of existing tenants. In addition, the leases for four other former Bradlees locations were assigned by Bradlees to other retailers. Of the remaining five locations which are currently vacant, two of the leases are guaranteed and the rent is being paid by Stop & Shop, a wholly-owned subsidiary of KoninKlijke Ahold NV (formerly Royal Ahold NV), an international food retailer. Stop & Shop remains contingently liable for rent at a number of the former Bradlees locations for the term of the Bradlees leases.

Property rentals for the year ended December 31, 2002, include \$5,000,000 of additional rent which was re-allocated to the former Bradlees locations in Marlton, Turnersville, Bensalem and Broomall and is payable by Stop & Shop, pursuant to the Master Agreement and Guaranty, dated May 1, 1992. This amount is in addition to all other rent guaranteed at the former Bradlees locations. On January 8, 2003, Stop & Shop filed a complaint with the United States District Court claiming the Company has no right to reallocate and therefore continue to collect the \$5,000,000 of annual rent from Stop & Shop because of the expiration of the East Brunswick, Jersey City, Middletown, Union and Woodbridge leases to which the \$5,000,000 of additional rent was previously allocated. The additional rent provision of the guaranty expires at the earliest in 2012. The Company intends to vigorously contest Stop & Shop's position.

In February 2003, KoninKlijke Ahold NV, parent of Stop & Shop, announced that it overstated its 2002 and 2001 earnings by at least \$500 million and is under investigation by the U.S. Justice Department and

Securities and Exchange Commission. The Company cannot predict what effect, if any, this situation involving KoninKlijke Ahold NV may have on Stop & Shop's ability to satisfy its obligation under the Bradlees guarantees and rent for existing Stop & Shop leases aggregating approximately \$10,500,000 million per annum.

Except for the U.S. Government, which accounted for 11.4% of the Company's revenue, none of the Company's other tenants represented more than 10% of total revenues for the year ended December 31, 2002.

As lessee:

The Company is a tenant under operating leases for certain properties. These leases will expire principally during the next thirty years. Future minimum lease payments under operating leases at December 31, 2002, are as follows:

(\$ in thousands)	
Year Ending December 31:	Amount
2003	\$ 15,347
2004	14,641
2005	14,644
2006	14,797
2007	14,762
Thereafter	954,980

Rent expense was \$17,157,000, \$15,433,000, and \$15,248,000 for the years ended December 31, 2002, 2001, and 2000.

11. COMMITMENTS AND CONTINGENCIES

At December 31, 2002, the Company's \$1,000,000,000 revolving credit facility had a zero balance, and the Company utilized \$9,112,000 of availability under the facility for letters of credit and guarantees. In addition there were \$7,667,000 of other letters of credit outstanding.

In conjunction with the closing of Alexander's Lexington Avenue construction loan on July 3, 2002, the Company agreed to guarantee, among other things, the lien free, timely completion of the construction of the project and funding of all project costs in excess of a stated budget, as defined in the loan agreement, if not funded by Alexander's (see Note 4—Investments in and Advances to Partially-Owned Entities).

Each of the Company's properties has been subjected to varying degrees of environmental assessment at various times. The environmental assessments did not reveal any material environmental contamination. However, there can be no assurance that the identification of new areas of contamination, changes in the extent or known scope of contamination, the discovery of additional sites, or changes in cleanup requirements would not result in significant costs to the Company.

The Company carries comprehensive liability and all risk property insurance (fire, flood, extended coverage and rental loss insurance) with respect to its assets. The Company's all risk insurance policies in effect before September 11, 2001 do not expressly exclude coverage for hostile acts, except for acts of war. Since September 11, 2001, insurance companies have for the most part excluded terrorist acts from coverage in all risk policies. The Company has generally been unable to obtain all risk insurance which

Vornado Realty Trust

includes coverage for terrorist acts for policies it has renewed since September 11, 2001, for each of its businesses. In 2002, the Company obtained \$200,000,000 of separate coverage for terrorist acts for each of its New York City Office, Washington, D.C. Office, Retail and Merchandise Mart businesses and \$60,000,000 for its Temperature Controlled Logistics business. Therefore, the Company is at risk for financial loss in excess of these limits for terrorist acts (as defined), which loss could be material.

The Company's debt instruments, consisting of mortgage loans secured by its properties (which are generally non-recourse to the Company), its senior unsecured notes due 2007 and its revolving credit agreement, contain customary covenants requiring the Company to maintain insurance. There can be no assurance that the lenders under these instruments will not take the position that an exclusion from all risk insurance coverage for losses due to terrorist acts is a breach of these debt instruments that allows the lenders to declare an event of default and accelerate repayment of debt. In the second quarter of 2002, the Company received correspondence from four lenders regarding terrorism insurance coverage, which the Company has responded to. In these letters the lenders took the position that under the agreements governing the loans provided by these lenders the Company was required to maintain terrorism insurance on the properties securing the various loans. The aggregate amount of borrowings under these loans as of December 31, 2002 was approximately \$770.4 million, and there was no additional borrowing capacity. Subsequently, the Company obtained an aggregate of \$360 million of separate coverage for "terrorist acts." To date, one of the lenders has acknowledged to the Company that it will not raise any further questions based on the Company's terrorism insurance coverage in place, and the other three lenders have not raised any further questions regarding the Company's insurance coverage. If lenders insist on greater coverage for these risks, it could adversely affect the Company's ability to finance and/or refinance its properties and to expand its portfolio.

From time to time, the Company has disposed of substantial amounts of real estate to third parties for which, as to certain properties, it remains contingently liable for rent payments or mortgage indebtedness.

There are various legal actions against the Company in the ordinary course of business. In the opinion of management, after consultation with legal counsel, the outcome of such matters will not have a material effect on the Company's financial condition, results of operations or cash flow.

The Company enters into agreements for the purchase and resale of U.S. government obligations for periods of up to one week. The obligations purchased under these agreements are held in safekeeping in the name of the Company by various money center banks. The Company has the right to demand additional collateral or return of these invested funds at any time the collateral value is less than 102% of the invested funds plus any accrued earnings thereon. The Company had \$33,393,000 and \$15,235,000 of cash invested in these agreements at December 31, 2002 and 2001.

12. RELATED PARTY TRANSACTIONS

Loan and Compensation Agreements

On May 29, 2002, Mr. Roth replaced common shares of the Company securing the Company's outstanding loan to Mr. Roth with options to purchase common shares of the Company with a value of not less than two times the loan amount. As a result of the decline in the value of the options, Mr. Roth supplemented the collateral with cash and marketable securities.

At December 31, 2002, the loan due from Mr. Roth in accordance with his employment arrangement was \$13,122,500 (\$4,704,500 of which is shown as a reduction in shareholders' equity). The loan bears interest at 4.49 % per annum (based on the applicable Federal rate) and matures in January 2006. The

Company also provided Mr. Roth with the right to draw up to \$15,000,000 of additional loans on a revolving basis. Each additional loan will bear interest, payable quarterly, at the applicable Federal rate on the date the loan is made and will mature on the sixth anniversary of the loan.

At December 31, 2002, loans due from Mr. Fascitelli, in accordance with his employment agreement, aggregated \$8,600,000. The loans which were scheduled to mature in 2003 have been extended to 2006 in connection with the extension of Mr. Fascitelli's employment agreement (discussed below), and bear interest, payable quarterly at a weighted average interest rate of 3.97% (based on the applicable Federal rate).

Pursuant to his 1996 employment agreement, Mr. Fascitelli became entitled to a deferred payment consisting of \$5 million in cash and a convertible obligation payable November 30, 2001, at the Company's option, in either 919,540 Company common shares or the cash equivalent of their appreciated value, so long as such appreciated value is not less than \$20 million. The Company delivered 919,540 shares to a rabbi trust upon execution of the 1996 employment agreement. The Company accounted for the stock compensation as a variable arrangement in accordance with Plan B of EITF No. 97-14 "Accounting for Deferred Compensation Arrangements Where Amounts Earned Are Held in a Rabbi Trust and Invested" as the agreement permitted settlement in either cash or common shares. Following the guidance in EITF 97-14, the Company recorded changes in fair value of its compensation obligation with a corresponding increase in the liability "Officer's Deferred Compensation". Effective as of June 7, 2001, the payment date was deferred until November 30, 2004. Effective as of December 14, 2001, the payment to Mr. Fascitelli was converted into an obligation to deliver a fixed number of shares (919,540 shares) establishing a measurement date for the Company's stock compensation obligation; accordingly the Company ceased accounting for the Rabbi Trust under Plan B of the EITF and began Plan A accounting. Under Plan A, the accumulated liability representing the value of the shares on December 14, 2001, was reclassified as a component of Shareholders' Equity as "Deferred compensation shares earned but not yet delivered." In addition, future changes in the value of the shares are no longer recognized as additional compensation expense. The fair value of this obligation was \$34,207,000 at December 31, 2002. The Company has reflected this liability as Deferred Compensation Shares Not Yet Delivered in the Shareholders' Equity section of the balance sheet. For the years ended December 31, 2001 and 2000, the Company recognized approximately \$4,744,000 and \$3,733,000 of compensation expense of which \$2,612,000 and \$1,968,000 represented the appreciation in value of the shares in each period and \$2,132,000 and \$1,765,000 represented dividends paid on the shares.

Effective January 1, 2002, the Company extended its employment agreement with Mr. Fascitelli for a five-year period through December 31, 2006. Pursuant to the extended employment agreement, Mr. Fascitelli is entitled to receive a deferred payment on December 31, 2006 of 626,566 Vornado common shares which are valued for compensation purposes at \$27,500,000 (the value of the shares on March 8, 2002, the date the extended employment agreement was executed). The shares are being held in a rabbi trust for the benefit of Mr. Fascitelli and vested 100% on December 31, 2002. The extended employment agreement does not permit diversification, allows settlement of the deferred compensation obligation by delivery of these shares only, and permits the deferred delivery of these shares. The value of these shares is being amortized ratably over the one year vesting period as compensation expense.

Pursuant to the Company's annual compensation review in February 2002 with Joseph Macnow, the Company's Chief Financial Officer, the Compensation Committee approved a \$2,000,000 loan to Mr. Macnow, bearing interest at the applicable federal rate of 4.65% per annum and due January 1, 2006. The loan, which was funded on July 23, 2002, was made in conjunction with Mr. Macnow's June 2002 exercise of options to purchase 225,000 shares of the Company's common stock. The loan is collateralized by assets with a value of not less than two times the loan amount. As a result of the decline in the value of the options, Mr. Macnow supplemented the collateral with cash and marketable securities.

Vornado Realty Trust

One other executive officer of the Company has a loan outstanding pursuant to an employment agreement totaling \$1,500,000 at December 31, 2002. The loan matures in April 2005 and bears interest at the applicable Federal rate provided (4.5% at December 31, 2002).

Transactions with Affiliates and Officers and Trustees of the Company

Alexander's

The Company owns 33.1% of Alexander's. Mr. Roth and Mr. Fascitelli are Officers and Directors of Alexander's and the Company provides various services to Alexander's in accordance with management and leasing agreements. See Note 4 "Investments in Partially-Owned Entities" for further details.

The Company constructed a \$16.3 million community facility and low-income residential housing development (the "30th Street Venture"), in order to receive 163,728 square feet of transferable development rights, generally referred to as "air rights." The Company donated the building to a charitable organization. The Company sold 106,796 square feet of these air rights to third parties at an average price of \$120 per square foot. An additional 28,821 square feet of air rights was purchased by Alexander's at a price of \$120 per square foot for use at Alexander's 59th Street development project (the "59th Street Project"). In each case, the Company received cash in exchange for air rights. The Company identified third party buyers for the remaining 28,111 square feet of air rights related to the 30th Street Venture. These third party buyers wanted to use the air rights for the development of two projects located in the general area of 86th Street which was not within the required geographical radius of the construction site nor in the same Community Board as the low-income housing and community facility project. The 30th Street Venture asked Alexander's to sell 28,111 square feet of the air rights it already owned to the third party buyers (who could use them) and the 30th Street Venture would replace them with 28,111 square feet of air rights. In October 2002, the Company sold 28,111 square feet of air rights to Alexander's for an aggregate purchase price of \$3,059,000 (an average of \$109 per square foot). Alexander's then sold an equal amount of air rights to the third party buyers for an aggregate purchase price of \$3,339,000 (an average of \$119 per square foot).

Interstate Properties

The Company currently manages and leases the real estate assets of Interstate Properties pursuant to a management agreement for which the Company receives an annual fee equal to 4% of base rent and percentage rent and certain other commissions. The management agreement has a term of one year and is automatically renewable unless terminated by either of the parties on sixty days' notice at the end of the term. Although the management agreement was not negotiated at arm's length, the Company believes based upon comparable fees charged by other real estate companies, that its terms are fair to the Company. For the years ended December 31, 2002, 2001, and 2000, \$1,450,000, \$1,655,000, and \$1,418,000 of management fees were earned by the Company pursuant to the management agreement.

Building Maintenance Service Company ("BMS")

On January 1, 2003, the Company acquired BMS, a company which provides cleaning and related services primarily to the Company's Manhattan office properties, for \$13,000,000 in cash from the estate of Bernard Mendik and certain other individuals including Mr. Greenbaum, an executive officer of the Company. The Company paid BMS \$53,024,000, \$51,280,000, and \$47,493,000 for the years ended December 31, 2002, 2001 and 2000 for services rendered to the Company's Manhattan office properties. Although the terms and conditions of the contracts pursuant to which these services were provided were not negotiated at arms length, the Company believes based upon comparable amounts charged to other real estate companies that the terms and conditions of the contracts were fair to the Company.

Vornado Operating Company

In October 1998, Vornado Operating Company (“Vornado Operating”) was spun off from the Company in order to own assets that the Company could not itself own and conduct activities that the Company could not itself conduct. The Company granted Vornado Operating a \$75,000,000 unsecured revolving credit facility (the “Revolving Credit Agreement”) which expires on December 31, 2004. Borrowings under the Revolving Credit Agreement bear interest at LIBOR plus 3%. The Company receives a commitment fee equal to 1% per annum on the average daily unused portion of the facility. No amortization is required to be paid under the Revolving Credit Agreement during its term. The Revolving Credit Agreement prohibits Vornado Operating from incurring indebtedness to third parties (other than certain purchase money debt and certain other exceptions) and prohibits Vornado Operating from paying dividends.

Vornado Operating has disclosed that in the aggregate its investments do not, and for the foreseeable future are not expected to, generate sufficient cash flow to pay all of its debts and expenses. Further, Vornado Operating states that its only investee, AmeriCold Logistics (“Tenant”), anticipates that its Landlord, a partnership 60% owned by the Company and 40% owned by Crescent Real Estate Equities, will need to restructure the leases between the Landlord and the Tenant to provide additional cash flow to the Tenant (the Landlord has previously restructured the leases to provide additional cash flow to the Tenant). Management anticipates a further lease restructuring and the sale and/or financing of assets by AmeriCold Logistics, and accordingly, Vornado Operating is expected to have a source to repay the debt under this facility, which may be extended. Since January 1, 2002, the Company has not recognized interest income on the debt under this facility.

Carthage, Missouri and Kansas City, Kansas Quarries

On December 31, 2002, the Company and Crescent Real Estate Equities formed a joint venture to acquire the Carthage, Missouri and Kansas City, Kansas quarries from AmeriCold Logistics, the tenant of the Temperature Controlled Logistics facilities for \$20,000,000 in cash. The Company contributed cash of \$8,800,000 to the joint venture representing its 44% interest. AmeriCold Logistics used the proceeds from the sale to repay a portion of a loan to Vornado Operating. Vornado Operating then repaid \$9,500,000 of the amount outstanding under the Company’s Revolving Credit Facility. On December 31, 2002, the joint venture purchased \$5,720,000 of trade receivables from AmeriCold Logistics at a 2% discount, of which the Company’s share was \$2,464,000.

Other

The Company owns preferred securities in Capital Trust, Inc. (“Capital Trust”) totaling \$29,212,000 at December 31, 2002. Mr. Roth, the Chairman and Chief Executive Officer of Vornado Realty Trust, is a member of the Board of Directors of Capital Trust.

On May 17, 2001, the Company sold its 50% interest in 570 Lexington Avenue to the other venture partner, an entity controlled by the late Bernard Mendik, a former trustee and executive officer of the Company, for \$60,000,000, resulting in a gain to the Company of \$12,445,000. The sale was initiated by the Company’s partner and was based on a competitive bidding process handled by an independent broker. The Company believes that the terms of the sale were at arm’s length and were fair to the Company.

During 2002 and 2001, the Company paid \$147,000 and \$136,000 for legal services to a firm in which one of the Company’s trustees is a member.

Vornado Realty Trust

On January 1, 2001, the Company acquired the common stock of various preferred stock affiliates which was owned by Officers and Trustees of the Company and converted them to taxable REIT subsidiaries. The total acquisition price was \$5,155,000. The purchase price, which was the estimated fair value, was determined by both independent appraisal and by reference to the individuals' pro rata share of the earnings of the preferred stock affiliates during the three-year period that these investments were held.

In connection with the Park Laurel condominium project, in 2001 the joint venture accrued \$5,779,000 of awards under the venture's incentive compensation plan.

13. MINORITY INTEREST

The minority interest represents limited partners', other than the Company, interests in the Operating Partnership and are comprised of:

Unit Series	Outstanding Units at		Per Unit Liquidation Preference	Preferred or Annual Distribution Rate	Conversion Rate Into Units
	December 31, 2002	December 31, 2001			
Common:					
Class A ⁽¹⁾	20,956,446	5,823,419	—	\$ 2.72	N/A
Convertible Preferred:					
5.0% B-1 Convertible Preferred	899,566	899,566	\$ 50.00	\$ 2.50	.914
8.0% B-2 Convertible Preferred	449,783	449,783	\$ 50.00	\$ 4.00	.914
6.5% C-1 Convertible Preferred	747,912	747,912	\$ 50.00	\$ 3.25	1.1431
6.5% E-1 Convertible Preferred	4,998,000	4,998,000	\$ 50.00	\$ 3.25 ⁽³⁾	1.1364
9.00% F-1 Preferred ⁽⁴⁾	400,000	400,000	\$ 25.00	\$ 2.25	— ⁽⁵⁾
Perpetual Preferred:⁽⁶⁾					
8.5% D-1 Cumulative Redeemable Preferred	3,500,000	3,500,000	\$ 25.00	\$ 2.125	N/A
8.375% D-2 Cumulative Redeemable Preferred	549,336	549,336	\$ 50.00	\$ 4.1875	N/A
8.25% D-3 Cumulative Redeemable Preferred	8,000,000	8,000,000	\$ 25.00	\$ 2.0625	N/A
8.25% D-4 Cumulative Redeemable Preferred	5,000,000	5,000,000	\$ 25.00	\$ 2.0625	N/A
8.25% D-5 Cumulative Redeemable Preferred	6,480,000	7,480,000	\$ 25.00	\$ 2.0625	N/A
8.25% D-6 Cumulative Redeemable Preferred	840,000	840,000	\$ 25.00	\$ 2.0625	N/A
8.25% D-7 Cumulative Redeemable Preferred	7,200,000	7,200,000	\$ 25.00	\$ 2.0625	N/A
8.25% D-8 Cumulative Redeemable Preferred	360,000	360,000	\$ 25.00	\$ 2.0625	N/A
8.25% D-9 Cumulative Redeemable Preferred	1,800,000	1,800,000	\$ 25.00	\$ 2.0625	N/A

⁽¹⁾ Class A units are redeemable at the option of the holder for common shares of beneficial interest in Vornado, on a one-for-one basis, or at the Company's option for cash.

⁽²⁾ Class D units automatically converted into Class A units in the third quarter of 2001. Prior to the conversion, the Class D unitholders participated in distributions at an annual rate of \$2.12, then *pari passu* with the Class A units.

⁽³⁾ Increases to \$3.38 in March 2006.

⁽⁴⁾ Issued in connection with the acquisition of a leasehold interest at 715 Lexington Avenue. Redeemable at the Company's option beginning January 2012 for Class A units.

⁽⁵⁾ Holders have the right to require the Company to redeem the outstanding F-1 units for cash equal to the Liquidation Preference of \$25.00 per share.

⁽⁶⁾ Convertible at the option of the holder for an equivalent amount of the Company's preferred shares and redeemable at the Company's option after the 5th anniversary of the date of issuance (ranging from December 1998 to September 2001).

14. INCOME PER SHARE

The following table sets forth the computation of basic and diluted income per share:

(Amounts in thousands, except per share amounts)	Year Ended December 31,		
	2002	2001	2000
Numerator:			
Income before gains on sale of real estate and cumulative effect of change in accounting principle	\$ 263,032	\$ 252,353	\$ 223,026
Gains on sale of real estate	—	15,495	10,965
Cumulative effect of change in accounting principle	(30,129)	(4,110)	—
Net income	232,903	263,738	233,991
Preferred stock dividends	(23,167)	(36,505)	(38,690)
Numerator for basic and diluted income per share— net income applicable to common shares	\$ 209,736	\$ 227,233	\$ 195,301
Denominator:			
Denominator for basic income per share— weighted average shares	105,889	89,109	86,521
Effect of dilutive securities:			
Employee stock options and restricted share awards	3,780	2,964	2,171
Denominator for diluted income per share— adjusted weighted average shares and assumed conversions	109,669	92,073	88,692
INCOME PER COMMON SHARE—BASIC:			
Income before gains on sale of real estate and cumulative effect of change in accounting principle	\$ 2.26	\$ 2.42	\$ 2.14
Gains on sale of real estate	—	.17	.12
Cumulative effect of change in accounting principle	(.28)	(.04)	—
Net income per common share	\$ 1.98	\$ 2.55	\$ 2.26
INCOME PER COMMON SHARE—DILUTED:			
Income before gains on sale of real estate and cumulative effect of change in accounting principle	\$ 2.18	\$ 2.34	\$ 2.08
Gains on sale of real estate	—	.17	.12
Cumulative effect of change in accounting principle	(.27)	(.04)	—
Net income per common share	\$ 1.91	\$ 2.47	\$ 2.20

Vornado Realty Trust

15. SUMMARY OF QUARTERLY RESULTS (UNAUDITED)

The following summary represents the results of operations for each quarter in 2002, 2001 and 2000:

(Amounts in thousands, except share amounts)	Revenue	Net Income Applicable to Common Shares	Net Income Per Common Share ⁽¹⁾	
		Basic	Diluted	
2002				
March 31	\$ 348,905	\$45,637 ⁽²⁾	\$.43 ⁽²⁾	\$.41 ⁽²⁾
June 30	355,763 ⁽²⁾	65,184 ⁽²⁾	.60 ⁽²⁾	.58 ⁽²⁾
September 30	363,571 ⁽²⁾	59,481 ⁽²⁾	.54 ⁽²⁾	.53 ⁽²⁾
December 31	366,831	39,434	.37	.36
2001				
March 31	\$ 242,610	\$46,836	\$.54	\$.52
June 30	246,075	56,920	.65	.64
September 30	250,265	67,876	.76	.74
December 31	246,823	55,601	.59	.57
2000				
March 31	\$ 195,279	\$47,523	\$.55	\$.54
June 30	198,745	47,281	.55	.53
September 30	215,655	58,447	.68	.65
December 31	216,293	42,050	.48	.47

⁽¹⁾ The total for the year may differ from the sum of the quarters as a result of weighting.

⁽²⁾ Restated to include the effect of SFAS 141—Business Combinations, for the amortization of above and below market leases acquired in 2002. The effect of restatement on each of the first three quarters on net income and net income per common share was \$940 or \$.02 per diluted share.

16. COSTS OF ACQUISITIONS AND DEVELOPMENT NOT CONSUMMATED

The Company has a 70% interest in a joint venture to develop an office tower over the Port Authority Bus Terminal in New York City. Current market conditions have resulted in the joint venture writing off \$9,700,000 in the fourth quarter of 2002, representing all pre-development costs capitalized to date, of which the Company's share is \$6,874,000.

In 2001, the Company was unable to reach a final agreement with the Port Authority of NY & NJ to conclude a net lease of the World Trade Center. Accordingly, the Company wrote-off costs of \$5,223,000 primarily associated with the World Trade Center.

17. SEGMENT INFORMATION

The Company has four business segments: Office, Retail, Merchandise Mart Properties and Temperature Controlled Logistics. Prior to 2001, income from the Company's preferred stock affiliates ("PSAs") was included in income from partially-owned entities. On January 1, 2001, the Company acquired the common stock of its PSAs and converted these entities to taxable REIT subsidiaries. Accordingly, the Hotel portion of the Hotel Pennsylvania and the management companies (which provide services to the Company's business segments and operate the Trade Show business of the Merchandise Mart division) have been consolidated effective January 1, 2001. Amounts for the years ended December 31, 2000 have been reclassified to give effect to the consolidation of these entities as if consolidated as of January 1, 2000. In addition, the Company has revised Adjusted EBITDA as previously reported for the year ended December 31, 2001 and 2000 to include income from the early extinguishment of debt of \$1,170,000 in 2001 and expense from the early extinguishment of debt of \$1,125,000 in 2000 because such items are no longer treated as extraordinary items in accordance with Generally Accepted Accounting Principles.

December 31, 2002

(\$ in thousands)	Total	Office	Retail	Merchandise Mart	Temperature Controlled Logistics	Other ⁽²⁾
Rentals	\$1,248,903	\$ 867,938	\$ 127,561	\$195,899	\$ —	\$ 57,505
Expense reimbursements	159,978	89,890	51,750	14,754	—	3,584
Other income	26,189	21,221	1,653	2,951	—	364
Total revenues	1,435,070	979,049	180,964	213,604	—	61,453
Operating expenses	541,596	343,723	65,455	86,022	—	46,396
Depreciation and amortization	205,826	146,746	15,507	26,716	—	16,857
General and administrative	98,458	34,346	5,036	20,382	—	38,694
Costs of acquisitions and development not consummated	6,874	—	—	—	—	6,874
Amortization of officers deferred compensation expense	27,500	—	—	—	—	27,500
Total expenses	880,254	524,815	85,998	133,120	—	136,321
Operating income	554,816	454,234	94,966	80,484	—	(74,868)
Income applicable to Alexander's	29,653	—	—	—	—	29,653
Income from partially-owned entities	44,458	1,966	(687)	(339)	9,707	33,811
Interest and other investment income	31,685	6,472	323	507	—	24,383
Interest and debt expense	(239,525)	(141,044)	(56,643)	(22,948)	—	(18,890)
Net gain on disposition of wholly-owned and partially-owned assets other than real estate	(17,471)	—	—	2,156	—	(19,627)
Minority interest	(140,584)	(119,910)	(13,736)	(23,910)	2,093	14,879
Income before gains on sale of real estate and cumulative effect of change in accounting principle	263,032	201,718	24,223	35,950	11,800	(10,659)
Gains on sale of real estate	—	—	—	—	—	—
Cumulative effect of change in accounting principle	(30,129)	—	—	—	(15,490)	(14,639)
Net income	232,903	201,718	24,223	35,950	(3,690)	(25,298)
Cumulative effect of change in accounting principle	30,129	—	—	—	15,490	14,639
Interest and debt expense ⁽³⁾	302,009	139,157	58,409	23,461	25,617	55,365
Depreciation and amortization ⁽³⁾	257,707	149,361	17,532	27,006	34,474	29,334
EBITDA	822,748	490,236	100,164	86,417	71,891	74,040
Adjustments:						
Minority interest	140,584	119,910	13,736	23,910	(2,093)	(14,879)
Gains (losses) on sale of real estate ⁽³⁾	(1,405)	—	—	—	2,026	(3,431)
Straight-lining of rents ⁽³⁾	(29,837)	(24,352)	(1,863)	(1,772)	—	(1,850)
Amortization of below market leases, net	(12,634)	(12,469)	(165)	—	—	—
Other	1,549	—	860	323	—	366
Adjusted EBITDA⁽¹⁾	\$ 921,005	\$ 573,325	\$ 112,732	\$ 108,878	\$ 71,824	\$ 54,246
Balance sheet data:						
Real estate, net	\$6,822,268	\$5,012,626	\$ 575,085	\$891,701	\$ —	\$342,856
Investments and advances to partially-owned entities	997,711	29,421	56,375	42,497	448,295	421,123
Capital expenditures:						
Acquisitions	2,739,746	2,650,298	89,448	—	—	—
Other	164,162	114,375	3,019	20,852	5,588	20,328

See notes on page 98.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *continued*

Vornado Realty Trust

December 31, 2001						
(\$ in thousands)	Total	Office	Retail	Merchandise Mart	Temperature Controlled Logistics	Other
Rentals	\$ 841,999	\$ 461,606	\$ 121,023	\$ 197,668	\$ —	\$ 61,702
Expense reimbursements	133,114	67,470	49,436	13,801	—	2,407
Other income	10,660	3,775	1,154	3,324	—	2,407
Total revenues	985,773	532,851	171,613	214,793	—	66,516
Operating expenses	398,969	217,581	56,547	83,107	—	41,734
Depreciation and amortization	123,862	71,425	14,767	25,397	—	12,273
General and administrative	72,572	12,421	3,576	18,081	—	38,494
Costs of acquisitions and development not consummated	5,223	—	—	—	—	5,223
Total expenses	600,626	301,427	74,890	126,585	—	97,724
Operating income	385,147	231,424	96,723	88,208	—	(31,208)
Income applicable to Alexander's	25,718	—	—	—	—	25,718
Income from partially-owned entities	80,612	32,746	1,914	149	17,447 ⁽⁴⁾	28,356
Interest and other investment income	54,385	6,866	608	2,045	—	44,866
Interest and debt expense	(173,076)	(54,667)	(55,358)	(33,354)	—	(29,697)
Net loss disposition of wholly-owned and partially-owned assets other than real estate	(8,070)	—	—	160	—	(8,230)
Minority interest	(112,363)	(55,932)	(16,562)	(15,650)	(10,968)	(13,251)
Income before gains on sale of real estate and cumulative effect of change in accounting	252,353	160,437	27,325	41,558	6,479	16,554
Gains on sales of real estate	15,495	12,445	3,050	—	—	—
Cumulative effect of change in accounting principle	(4,110)	—	—	—	—	(4,110)
Net income	263,738	172,882	30,375	41,558	6,479	12,444
Cumulative effect of change in accounting principle	4,110	—	—	—	—	4,110
Interest and debt expense ⁽⁵⁾	266,784	92,410	57,915	33,354	26,459	56,646
Depreciation and amortization ⁽⁵⁾	188,859	91,085	18,957	25,397	33,815	19,605
EBITDA	723,491	356,377	107,247	100,309	66,753	92,805
Adjustments:						
Gains on sale of real estate ⁽⁵⁾	(21,793)	(12,445)	(3,050)	—	—	(6,298)
Minority interest	112,363	55,932	16,562	15,650	10,968	13,251
Net gain on disposition of wholly-owned and partially-owned assets other than real estate	(160)	—	—	(160)	—	—
Straight-lining of rents ⁽⁵⁾	(26,134)	(20,064)	727	(4,997)	—	(1,800)
Other	(2,715)	—	(2,337)	—	716	(1,094)
Adjusted EBITDA⁽¹⁾	\$ 785,052	\$ 379,800	\$ 119,149	\$ 110,802	\$ 78,437	\$ 96,864
Balance sheet data:						
Real estate, net	\$ 4,183,986	\$ 2,446,534	\$ 503,923	\$ 911,067	\$ —	\$ 322,462
Investments and advances to partially-owned entities	1,270,195	374,371	28,213	9,764	474,862	382,985
Capital expenditures:						
Acquisitions	11,574	11,574	—	—	—	—
Other	158,343	79,117	7,597	51,036	5,700	14,893

See notes on page 98.

December 31, 2000
(after giving effect to consolidation of PSAs)

(\$ in thousands)	Total	Office	Retail	Merchandise Mart	Temperature Controlled Logistics	Other ⁽²⁾
Rentals	\$ 788,469	\$ 406,261	\$ 129,902	\$ 171,001	\$ —	\$ 81,305
Expense reimbursements	120,074	60,767	45,490	10,654	—	3,163
Other income	17,608	5,499	2,395	4,661	—	5,053
Total revenues	926,151	472,527	177,787	186,316	—	89,521
Operating expenses	379,524	199,424	55,671	74,553	—	49,876
Depreciation and amortization	108,109	58,074	17,464	21,984	—	10,587
General and administrative	63,468	10,401	667	16,330	—	36,070
Total expenses	551,101	267,899	73,802	112,867	—	96,533
Operating income	375,050	204,628	103,985	73,449	—	(7,012)
Income applicable to Alexander's	17,363	—	—	—	—	17,363
Income from partially-owned entities	79,694	29,210	667	—	28,778 ⁽⁴⁾	21,039
Interest and other investment income	33,798	6,162	—	2,346	—	25,290
Interest and debt expense	(180,505)	(62,162)	(54,305)	(38,569)	—	(25,469)
Minority interest	(102,374)	(46,917)	(16,550)	(12,660)	(12,483)	(13,764)
Income before gains on sale of real estate	223,026	130,921	33,797	24,566	16,295	17,447
Gains on sale of real estate	10,965	8,405	2,560	—	—	—
Net income	233,991	139,326	36,357	24,566	16,295	17,447
Interest and debt expense ⁽³⁾	260,573	96,224	55,741	38,566	27,424	42,618
Depreciation and amortization ⁽³⁾	167,268	76,696	18,522	20,627	34,015	17,408
EBITDA	661,832	312,246	110,620	83,759	77,734	77,473
Adjustments:						
Minority interest	102,374	46,917	16,550	12,660	12,483	13,764
Gains on sale of real estate ⁽³⁾	(10,965)	(8,405)	(2,560)	—	—	—
Straight-lining of rents ⁽³⁾	(30,001)	(19,733)	(2,295)	(5,919)	(1,121)	(933)
Other	14,510	—	(1,654)	1,358	4,064 ⁽²⁾	10,742 ⁽⁵⁾
Adjusted EBITDA⁽¹⁾	\$ 737,750	\$ 331,025	\$ 120,661	\$ 91,858	\$ 93,160	\$101,046
Balance sheet data:						
Real estate, net	\$ 3,960,605	\$ 2,388,393	\$ 551,183	\$ 862,003	\$ —	\$ 159,026
Investments and advances to partially-owned entities	1,459,211	394,089	31,660	41,670	469,613	522,179
Capital expenditures:						
Acquisitions	246,500	128,000	—	89,000	—	29,500
Other	212,907	106,689	7,251	37,362	28,582	33,023

See notes on following page.

Vornado Realty Trust

Notes:

⁽¹⁾ *Adjusted EBITDA represents EBITDA adjusted for gains or losses on sales of depreciable real estate, the effect of straight-lining of rent escalations, amortization of acquired above and below market leases and minority interest. Management considers Adjusted EBITDA a supplemental measure for making decisions and assessing the performance of its segments. Adjusted EBITDA should not be considered a substitute for net income or a substitute for cash flow as a measure of liquidity. Adjusted EBITDA is presented as a measure of "operating performance" which enables the reader to identify trends from period to period and may be used to compare "same store" operating performance to other companies, as well as providing a measure for determining funds available to service debt. Adjusted EBITDA may not be comparable to similarly titled measures employed by other companies.*

⁽²⁾ *Adjusted EBITDA—Other is comprised of:*

(Amounts in thousands)	For the Year Ended December 31,		
	2002	2001	2000
Hotel Pennsylvania	\$ 7,636	\$ 16,978	\$ 26,866
Newkirk Joint Ventures:			
Equity in income of limited partnerships	60,756	54,695	43,685
Interest and other income	8,795	8,700	7,300
Alexander's	34,381	19,362	18,330
Investment income and other	31,261	44,097	34,990
Unallocated general and administrative expenses	(34,743)	(33,515)	(30,125)
Primestone foreclosure and impairment loss.	(35,757)	—	—
Amortization of Officer's deferred compensation expense	(27,500)	—	—
Net gain on sale of marketable securities	12,346	—	—
Write-off of 20 Times Square pre-development costs (2002) and World Trade Center acquisition costs (2001)	(6,874)	(5,223)	—
Net gain on sale of air rights.	1,688	—	—
Gain on transfer of mortgages	2,096	—	—
Palisades	161	—	—
After-tax net gain on sale of Park Laurel condominium units	—	15,657	—
Write-off of net investment in Russian Tea Room ("RTR")	—	(7,374)	—
Write-off of investments in technology companies	—	(16,513)	—
Total	\$ 54,246	\$ 96,864	\$101,046

⁽³⁾ *Interest and debt expense, depreciation and amortization, straight-lining of rents and gains on sale of real estate included in the reconciliation of net income to EBITDA or Adjusted EBITDA reflects amounts which are netted in income from partially-owned entities.*

⁽⁴⁾ *Excludes rent not recognized of \$19,348, \$15,281 and \$9,787 for the years ended December 31, 2002, 2001 and 2000.*

⁽⁵⁾ *Includes the reversal of \$1,266 and \$4,765 of expenses in 2001 and 2000 representing the non-cash appreciation in the value of shares held in a rabbi trust in connection with a deferred compensation arrangement for the Company's President.*

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INDEPENDENT AUDITORS' REPORT

Shareholders and Board of Trustees
Vornado Realty Trust
New York, New York

We have audited the accompanying consolidated balance sheets of Vornado Realty Trust as of December 31, 2002 and 2001, and the related consolidated statements of income, shareholders' equity, and cash flows for each of the three years in the period ended December 31, 2002. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, such consolidated financial statements present fairly, in all material respects, the financial position of Vornado Realty Trust at December 31, 2002 and 2001, and the results of its operations and its cash flows for each of the three years in the period ended December 31, 2002, in conformity with accounting principles generally accepted in the United States of America.

As discussed in Note 2 to the consolidated financial statements, on January 1, 2002, the Company adopted the provisions of *Statement of Financial Accounting Standards No. 142 "Goodwill and Other Intangible Assets."*

DELOITTE & TOUCHE LLP

Parsippany, New Jersey
March 6, 2003

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MARKET PRICE OF VORNADO COMMON STOCK AND RELATED INFORMATION

Vornado Realty Trust

Vornado's common shares are traded on the New York Stock Exchange under the symbol "VNO."

Quarterly closing price ranges of the common shares and dividends paid per share for the years ended December 31, 2002 and 2001 were as follows:

Quarter	Year Ended December 31, 2002			Year Ended December 31, 2001		
	High	Low	Dividends	High	Low	Dividends
1st	\$44.90	\$41.78	\$.66	\$38.76	\$34.57	\$.53
2nd	47.10	43.02	.66	39.75	34.56	.53
3rd	45.38	37.65	.66	41.60	37.95	.60
4th	39.21	34.41	.68	41.65	37.60	.97*

* Comprised of a regular quarterly dividend of \$.66 per share and a special dividend of \$.31 declared on December 18, 2001, which was necessary to avoid the Company incurring an excise tax on distributions of less than 85% of taxable income in the current year.

On March 3, 2003, there were 1,750 holders of record of the Company's common shares.

At December 31, 2002, the Company had a capital loss carryover of approximately \$73,000,000. The capital loss carryover is available to offset future capital gains that would otherwise be required to be distributed as dividends to shareholders.

Recent Sales of Unregistered Securities

During 2002, 2001 and 2000 the Company issued 176,848, 6,002 and 2,357 common shares, respectively, upon the redemption of Class A units of the Operating Partnership held by persons who received units in private placements in earlier periods in exchange for their interests in limited partnerships that owned real estate. The common shares were issued without registration under the Securities Act of 1933 in reliance on Section 4(2) of that Act.

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VORNADO CORPORATE INFORMATION

TRUSTEES

STEVEN ROTH

*Chairman of the Board
Managing Partner, Interstate Properties*

MICHAEL D. FASCITELLI

President

ROBERT P. KOGOD

DAVID M. MANDELBAUM*

Partner, Interstate Properties

STANLEY SIMON*

*Principal, Stanley Simon and Associates,
Management and Financial Consultants*

ROBERT H. SMITH

*Chairman of Charles E. Smith Commercial Realty,
a division of Vornado Realty Trust*

RONALD G. TARGAN

President, Malt Products Corporation

RICHARD R. WEST*

*Dean Emeritus, Leonard N. Stern School of Business,
New York University*

RUSSELL B. WIGHT, JR.

Partner, Interstate Properties

**Members of the Audit Committee*

OFFICERS

STEVEN ROTH

*Chairman of the Board and
Chief Executive Officer*

MICHAEL D. FASCITELLI

President

MELVYN H. BLUM

*Executive Vice President—
Development*

ALEC C. COVINGTON

*President and Chief Executive Officer of
Temperature Controlled Logistics*

MICHELLE FELMAN

*Executive Vice President—
Acquisitions*

DAVID R. GREENBAUM

*President of the
New York Office Division*

CHRISTOPHER KENNEDY

*President of the
Merchandise Mart Division*

PAUL LARNER

*Executive Vice-President—
Chief Administrative Officer and Secretary*

JOSEPH MACNOW

*Executive Vice President—
Finance and Administration and
Chief Financial Officer*

SANDEEP MATHRANI

*Executive Vice President—
Retail Real Estate Division*

MITCHELL N. SCHEAR

*President of Charles E. Smith Commercial Realty,
a division of Vornado Realty Trust*

WENDY SILVERSTEIN

*Executive Vice President—
Capital Markets*

COMPANY DATA

EXECUTIVE OFFICES

888 Seventh Avenue
New York, New York 10019

INDEPENDENT AUDITORS

Deloitte & Touche LLP
Parsippany, New Jersey

GENERAL COUNSEL

Sullivan & Cromwell
New York, New York

TRANSFER AGENT AND REGISTRAR

First Union National Bank
Charlotte, North Carolina

REPORT 10-K

Shareholders may obtain a copy of the Company's annual report on Form 10-K as filed with the Securities and Exchange Commission free of charge (except for exhibits), by writing to the Secretary, Vornado Realty Trust, 210 Route 4 East, Paramus, New Jersey 07652; or, visit the Company's website at www.vno.com and refer to the Company's SEC Filings

ANNUAL MEETING

The annual meeting of shareholders of Vornado Realty Trust, will be held at 12:00 noon on Wednesday, May 28, 2003 at the Marriott Hotel, Interstate 80 and the Garden State Parkway, Saddle Brook, New Jersey 07663

